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IN THE

Supreme Court of the United States

October Term, 1971

Docket No. 71 - 421

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

WALTER A. MITCHELL,
Respondent.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

GEORGE GORDON REYNOLDS,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

To the Honorable Warren E. Burger, Chief Justice, and the Honorable Associate Justices of the Supreme Court of the United States:

Your petitioners, Texas Gulf Sulphur Company and Charles F. Fogarty, respectfully pray that a writ of certiorari issue to review the judgment of the United States

Court of Appeals for the Tenth Circuit entered in this proceeding on April 26, 1971. The decision below is based largely on language in the Second Circuit opinion in *Securities and Exchange Commission* v. *Texas Gulf Sulphur Company*, in which petitions seeking review in this Court have been filed by these petitioners and others (Nos. 327, 328, 346, 347).

Opinions Below

The opinion of the United States District Court for the District of Utah (Ritter, J.) is reported at 309 F. Supp. 548 and at page 1a.* The opinion of Circuit Judge Hill for the Tenth Circuit Court of Appeals, not yet officially reported, appears at page 40a.

Jurisdiction

The judgments of the Court of Appeals were entered on April 26, 1971. A timely petition for rehearing by respondents was denied on September 10, 1971, and this petition for certiorari was filed within ninety days of the latter date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

Questions Presented

1. Whether a corporate press release warning against false and extravagant rumors concerning operations of the company was issued "in connection with the purchase or sale of any security" (thereby coming within the ambit of Section 10(b) of the Securities Exchange Act of 1934 and

* References in this form are to the Appendix annexed hereto.

Rule 10b-5 thereunder) when neither the company nor those who prepared the release were buying or selling its securities and did not intend, expect or receive any advantage from the release?

2. Whether, without proof of intent to deceive, a company and its officers should be held liable under the statute and rule in damages for a press release which expressed the good faith opinion of responsible corporate management with respect to preliminary evaluation of a mineral prospect and which promised a detailed statement "as soon as reasonable and logical conclusions can be made"?

3. Whether, on the facts at bar, a private cause of action should be implied from a rule promulgated by an administrative agency, when such an implication is contrary to the legislative scheme and when to do so will discourage the disclosure of information to the public and thus thwart one of the principal goals of the securities laws?

4. Whether, when neither fraud nor reckless conduct was shown, the First Amendment rights of petitioners to comment on a matter of public interest were abridged by the decision below?

5. Whether, when the company issued a second press release which was relayed to every brokerage house in the country and which provided detailed information regarding an ore discovery, persons who sold the company's stock after the second release had been received by their brokers should be permitted to recover hypothetical additional

profits from the company based upon their own testimony that their sales were prompted by a prior release which had not provided detailed information but which had promised the second release?

6. What measure of damages should be awarded a seller claiming lost speculative profits where the stock is traded on a national exchange and numerous factors have been responsible for a large increase in market price?

7. Whether, if a showing of fraud is not required for the imposition of liability in damages under Rule 10b-5, the statute of limitations to be applied should, nevertheless, be based on state fraud provisions rather than state blue-sky or other statutes which contain similar substantive language?

8. Whether, under the provisions of Section 27 of the Securities Exchange Act of 1934, there is jurisdiction in the District of Utah over the person of a corporate official who is not found, is not an inhabitant, and transacts no business in the district, and whose sole act was, as part of his duties with a corporation, to draft a press release in New York, reports of which were subsequently disseminated by the news media throughout the United States including Utah.

Statutes and Rule Involved

48 Stat. 891, 902; 15 U.S.C. §§78j(b), 78aa are set forth at pages 75a-76a of Appendix B to this Petition.

17 C.F.R. §240.10b-5 is set forth at page 76a of Appendix B to this Petition.

Statement of the Case

A. Introductory Statement

These actions arose out of the issuance of a press release on April 12, 1964 by Texas Gulf Sulphur Company ("Texas Gulf") commenting on published rumors concerning its mineral exploration activities near Timmins, Ontario, Canada. While the monetary amounts involved in these actions are not large, the legal principles and impact of this case are of great significance. The decisions below, for the first time, apply to a private damage action the legal conclusions reached by the Second Circuit in *SEC* v. *Texas Gulf Sulphur Company,* 401 F.2d 833 (2d Cir. 1968) (the "SEC action"). They mark the culmination of a process whereby private causes of action, not granted by Congress when it created certain private causes of action under the Securities Exchange Act, have been judicially implied for violation of a rule promulgated by an administrative agency.

While the *SEC* action did not itself involve private claims for damages, Judge Friendly, in a concurring opinion, identified the damage question as one "transcending in public importance all others in this important case". He stated persuasively, from reason and the legislative history, that "the April 12 press release would be the worst possible case for the award of damages" because of its punitive effect on the company's innocent shareholders and its inhibitory effect on dissemination of information "to security holders and the public generally with respect to important business and financial developments" (401 F.2d at 866, 868, 867). Judge Friendly went on to point out that the Rule, at least as later construed by the Tenth

Circuit herein, might well be beyond the authority vested in the SEC by §10(b) and be so inconsistent with the statutory structure as to be impermissible (401 F.2d at 868).

Moreover, while the present actions involve only two plaintiffs, a class action is pending in the Southern District of New York based on similar allegations on behalf of all sellers of Texas Gulf Stock after issuance of the April 12 release and before publication of a second release announcing a major discovery. See *Cannon* v. *Texas Gulf Sulphur Co.*, 47 F.R.D. 60 (S.D.N.Y. 1969). As the Court of Appeals below noted, if damages were to be awarded in that action on the basis of the principles adopted below, the recovery would amount to millions of dollars (66a-67a). Yet in neither the *SEC* action nor this action was any evidence adduced of any intentional wrongdoing in connection with the press release or of any economic benefit to the corporation, its stockholders or its employees from its issuance. As Judge Friendly stated, to award damages in this context is "frightening", not only for Texas Gulf, but for all publicly held corporations. 401 F.2d at 866.

The questions presented by this petition and the companion petitions in the *SEC* action raise important and far-reaching questions under the securities laws concerning disclosure of information relating to corporate activities, questions upon which this Court has not yet passed. The decisions below run counter to a basic purpose of those laws, and should now be reviewed by this Court. Judge Friendly believed it incumbent upon the Second Circuit to give guidance to the district courts upon these problems (401 F.2d at 866), but that court failed to do so. It is now imperative that such guidance be supplied by this Court.

B. The Proceedings Below

Respondents Reynolds and Mitchell instituted actions in the Utah District Court against petitioners on July 12, 1966, and April 17, 1967, respectively. They sought to recover damages upon sales of stock allegedly induced by violations of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b) (the "1934 Act") and Rule 10b-5, 17 C.F.R. §240.10b-5, promulgated thereunder. Jurisdiction of the District Court was invoked under Section 27 of the 1934 Act, 15 U.S.C. §78aa.

The press release of April 12, 1964, of which respondents complain, was followed four days later on the morning of April 16 by a second release announcing a major mineral discovery. Respondent Reynolds sold TGS stock on April 16, and respondent Mitchell on April 17 and April 23, all sales taking place *after* the second release had been received by their brokers and after a sharp rise in the price of Texas Gulf stock. Both respondents claimed, however, that their sales were caused by and made in reliance upon the earlier (April 12) press release and that their shares were sold to petitioner Fogarty.

The actions were consolidated (with two other actions not involved in this petition) and tried before the court without a jury. Judgments were awarded to respondents, and on appeal the judgment in favor of Reynolds was affirmed in all respects except as to the issue of damages; the judgment in favor of Mitchell was affirmed in all respects except as to damages and as to his sale of 20 shares of stock. The Court of Appeals ordered that the cases be remanded with directions to enter judgment in higher

amounts, for Reynolds in the amount of $12,687.50, and to Mitchell for $7,600.00, both to receive interest on those amounts from the dates of their sales in April of 1964.

C. The Facts

The evidence was uncontradicted that the April 12 press release was issued because of the front page appearance in the New York newspapers on Saturday, April 11, 1964, of false statements concerning Texas Gulf's drilling activities, and rumors that Texas Gulf and an alleged partner had made "the biggest ore strike since gold was discovered more than 60 years ago in Canada," a "sensational copper strike" and similar superlatives. After consultation among President Stephens, Executive Vice President Fogarty and the company's public relations consultant, it was concluded that TGS should promptly put out a press release in response to the rumors. A draft of the release was prepared on Saturday and Sunday by Dr. Fogarty, after telephone conversations and meetings with Richard D. Mollison, the Texas Gulf vice president in direct charge of the project who had been on the property the previous day, April 10. Mollison supplied the available information and with that, Fogarty prepared the first draft of the release. It was put in final form by Texas Gulf's public relations consultant and, after Dr. Fogarty had conferred with President Stephens and a Texas Gulf attorney, President Stephens authorized its issuance (43a-44a).

The Court of Appeals recognized that at the time the press release was drafted "[t]he president, a vice president and Fogarty all agreed that they could not responsibly conclude that a commercial ore body existed and that no

calculations as to the size or grade of ore could be made without further drilling" (44a). This conclusion was concurred in by the eminent mining experts called by defendants at trial. In these circumstances, Texas Gulf chose to issue a statement which did not set forth detailed drilling information, but rather rebutted the falsehoods and warned of the exaggerations. It not only stated that the work done to date had "not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly misleading," but also promised that when Texas Gulf had "progressed to the point where reasonable and logical conclusions can be made, TGS will issue a definite statement to its stockholders and to the public in order to clarify the Timmins project" (44a-45a, n.5).

The April 12 release was reported on in several newspapers, including the *Wall Street Journal,* on Monday morning, April 13, and by the Dow-Jones news service. On that day, TGS stock closed at $30⅞, 75 cents above its closing price the previous trading day, April 10.

On Sunday, April 12, contemporaneously with the issuance of the release, Texas Gulf sent the officials in charge of its exploration team back to Timmins from New York. A fourth drilling rig was put into operation—until April 8 only one had been able to operate because of a shortage of water—and the drilling progress was accelerating. By the afternoon of Wednesday, April 15, four more holes had been completed to add to the three which had been completed by April 10, and twice as much footage had been drilled as

on the 10th. Moreover, the holes covered a much larger area, giving meaningful results on April 15 over a space four times as large as had been drilled on April 10. Thus, on April 16, TGS was able to issue the definite statement promised by the April 12 release; this release commenced with the statement that TGS "has made a major discovery of zinc, copper and silver in the Timmins area of Ontario, Canada."

The second release was carried over the private wire of Reynolds' broker, Merrill Lynch, and received in Salt Lake City at 8:29 A.M., M.S.T., on April 16. The Dow-Jones news service also carried the story to the brokerage houses in Utah at 8:55 A.M., M.S.T., and the April 16 press release received wide coverage in newspapers throughout the country (46a).

Respondent Reynolds, a Salt Lake City resident, testified that after he had read reports of the April 12 release on Monday, April 13, and discussed them with his broker, he decided not to sell but instead to "hold the stock, see what happened." He gave his order to sell only after his Merrill Lynch representative had called him on the morning of April 16, *after* the reports of the April 16 release had been conveyed to Merrill Lynch in Salt Lake City, and *after* he had been informed by his broker that "there's a rumor that Texas Gulf has made a big strike." Reynolds' stock was sold for $33\frac{5}{8}$ per share at 9:31 A.M., M.S.T., an hour after the Merrill Lynch wire had been received in Salt Lake City (20a-21a).

Respondent Mitchell, a Los Angeles resident, who made a habit of coming into his broker's office "almost daily"

and reading the "Dow-Jones broad tape," nevertheless testified that he first learned of the *April 12* release on April 16 at 9:30 A.M., P.S.T. at his broker's office. This was 1½ hours *after* news of the *April 16* release had there been received, posted, and generally made available to the customers. Mitchell saw the hectic trading and rise in price in TGS stock that morning, returned to his office and reviewed his TGS file, and then went to the offices of another broker and placed an unsolicited order for the sale of 400 shares of TGS stock. This was no ordinary sale order: rather it was an order for a short sale against the box at $40.00 per share, although at the time this order was entered, the stock was trading at $34½ to $34¾. The stock was sold on the next day, April 17, for $40, $10 above the price before the April 12 release was issued. Subsequently, Mitchell placed another order for a short sale against the box at a price of $45.00 per share, and the shares were actually sold on April 23 for $46¼. He nevertheless asserted that his sales orders, placed substantially above the market, were made in reliance upon and induced by the earlier April 12 release (23a-24a).

D. The Decisions Below

These actions were tried April 29 through May 2, 1968. More than sixteen months later, on September 11, 1969, and after the intervening decision of the Second Circuit in the *SEC* action, Judge Ritter announced his decision in favor of respondents. An opinion was filed on October 17, 1969, and a revised opinion, along with amended findings of fact and conclusions of law, was filed on January 9, 1970.

In his revised opinion, Judge Ritter held that both Texas Gulf and Dr. Fogarty had violated §10(b) and Rule 10b-5 in issuing the press release. However, he rejected respondents' charges that the release was the product of a conspiracy to depress the price of the stock for the benefit of petitioners, that it was issued for the purpose of enabling certain persons, including petitioners, to purchase shares of TGS stock cheaply, and that Dr. Fogarty had purchased respondents' stock. Judge Ritter said, however, that the press release was "inaccurate, misleading and deceptive with respect to material matters disclosed by the company's drilling near Timmins," and added in his opinion (although not in the findings) that "the court thinks designedly so" (21a, 25a). No evidentiary support nor any basis for the last statement was cited, and none exists in the record.

The District Court further held that despite the fact that the sales had taken place *after* dissemination of the second press release of April 16, 1964, respondents had relied on the first release in making their sales. Damages were awarded based on a measure of the difference between their sales prices and the average of the highest daily prices of Texas Gulf stock for a month (twenty trading days) after the April 16 announcement.

On appeal the Court of Appeals affirmed, relying heavily, as had the District Court, on the opinion of the Second Circuit in the *SEC* action. The Court of Appeals found that the general language of Rule 10b-5 prohibited the "wait and see" release of April 12, *i.e.*, that when Texas Gulf and Fogarty "undertook to deny and clarify rumor and fact, they were bound to accurately depict the situation as they then knew it" (53a). Moreover, although the

court recognized that the principal officers of Texas Gulf in charge of the exploration "could not responsibly conclude that a commercial ore body existed and no * * * calculation as to size or grade of ore could be made without further drilling," nevertheless it held that a statement to that effect was not legally sufficient and that Texas Gulf was required to set forth "the then known dimensions and drilling data of their discovery" (44a, 53a). The Tenth Circuit further held that the press release was issued "in connection with" the purchase and sale of securities, although there had been no showing that either the corporation or any insiders were in the market for stock and no showing that the press release was designed to affect the market price of Texas Gulf stock for the benefit of the corporation or any insiders.

The Tenth Circuit apparently found no basis for the District Court's unsupported speculation that the press release was "intentionally deceptive * * * and knowingly deficient." However, undeterred by this lack of evidentiary support, the Tenth Circuit simply switched the burden of proof on this issue to defendants, and held that "[c]onfronted with the abundance of evidence in the record,"* it could not be concluded that Texas Gulf had "sustained its burden of proving that it did not know of the misrepresentation" (61a).

As to respondents' supposed "reliance," the Tenth Circuit stated that "the evidence is not so deficient as to make the finding of the trial court clearly erroneous that the principal reliance was on the April 12 statement" (62a). However, the court felt that the issuance of the April 16 release

* What this "abundance of evidence" consisted of was never explicitly stated and the record will be searched in vain for any evidence of bad faith or intentional deception.

should bar recovery for sales made "at some point in time after [its] publication" (63a). Despite the "abundance of publicity given the April 16 statement" and the massive trading immediately after its dissemination, the court felt that only claims made on sales after April 20 (including one involving 20 shares by respondent Mitchell on April 23) should be barred from recovery.

With respect to damages, the Court of Appeals, admittedly fashioning a new rule, held that respondents should be permitted to recover the difference between the prices for which their shares were sold and the highest value between April 20 (*i.e.*, the date when, the court speculated, "the diligent and reasonable investor was informed of the most recent Texas Gulf statement") and a date ending the period within which, after being informed, the reasonable investor is to be permitted "to decide whether or not he would reinvest and take advantage of a spiraling market" (67a). This measure of damages led to an increase of approximately 50% in the awards to Reynolds and Mitchell over the amounts ordered by the District Court, which were based on the average high prices for the stock over a period of one month.

Reasons for Allowance of the Writ

1. The Tenth Circuit has decided questions of federal substantive law under the securities laws which are of great importance and wide application to all corporations whose stock is publicly traded, to their shareholders, and to the public generally, and which should be settled by this Court. In particular, the Tenth Circuit, in an unprecedented decision, has held that a corporation, which

chooses to issue a press release in good faith and without ulterior purpose in response to false and exaggerated published rumors, can be held liable in damages to sellers of stock who claim to have been discouraged thereby. This holding makes the corporation's present shareholders insurers for the hypothetical profits of former shareholders. The decision, if permitted to stand, will inhibit disclosure of information about corporate activities where no statement is legally required and thus frustrate, not further, one of the principal goals of the securities laws.

2. The decision below is inconsistent with the express provisions of the 1933 and 1934 Acts establishing private causes of action since it permits recovery of damages in the absence of an affirmative showing of fraud and of petitioners' involvement in securities transactions.

3. The decision below is in conflict with rulings of the Second Circuit that damages may not be awarded in private actions under Rule 10b-5 without proof of *scienter*. The decision also violates petitioners' rights under the First Amendment.

4. In conflict with a decision of the Eighth Circuit Court of Appeals, the Tenth Circuit has held, despite its holding that plaintiffs need not demonstrate fraud to recover, that the "most nearly analogous" statute of limitations is the state fraud statute, rather than the state "blue-sky" provision which contains language similar to Rule 10b-5.

5. The Court of Appeals has, in conflict with decisions of this Court, sustained jurisdiction over the individual petitioner despite the lack of evidence that he had any purposeful connection with the state in which the district lies.

ARGUMENT

I

The Court of Appeals, in awarding damages against petitioners for good faith issuance of a press release, found to be defective for failure to conform to standards first enunciated in this litigation, has contravened all prior precedent and legislative history and has rendered a decision in conflict with the basic structure and purpose of the securities laws.

A. The press release was not issued "in connection with" the purchase or sale of securities simply because it was issued by a company whose stock is publicly traded.

Section 10(b) of the 1934 Act was designed by Congress to enable the Securities and Exchange Commission to deal with manipulative or deceptive devices integrally related to transactions in securities, not to serve as the basis for regulating corporate comment which is unrelated to securities transactions. Certain aspects of corporate disclosure were dealt with specifically in the 1934 Act in Sections 12, 14, 16(a), 18 and 32, and disclosure by registration statement and prospectus was the subject of the 1933 Act. Section 10(b), on the other hand, was meant to be a supplement to the specific prohibitions against manipulation by traders and other market professionals contained in Sections 9 and 10(a) of the 1934 Act as the legislative history clearly demonstrates. One of the principal draftsmen of the 1934 Act testified:

> "Subsection [b] says, 'Thou shalt not devise any other cunning devices' * * * Of course subsection [b] is a

> catch-all clause to prevent manipulative devices. I do not think there is any objection to that kind of a clause. The Commission should have the authority to deal with new manipulative devices." Testimony of Thomas G. Corcoran, *Hearings on H.R. 7852 and H.R. 8720 before the House Committee on Interstate and Foreign Commerce,* 73d Cong., 2d Sess. 115 (1934).

The manipulative devices outlawed by Section 9 all involve fraudulent activities integrally related to securities transactions: matched orders, pools, wash sales and the like. In enacting §10(b), as well as the other antifraud provisions of the securities laws—Sections 12(2) and 17(a) of the 1933 Act and Section 15(c)(1) of the 1934 Act—Congress' concern was to enable the SEC to deal with purposeful schemes by purchasers or sellers to defraud the public by means of manipulative and deceptive devices. No such activity was involved here.

The case law, prior to the *SEC* action, was in accord with this legislative purpose. Satisfaction of the "in connection with" requirement, it was repeatedly held, required a showing by plaintiff that defendant had either (1) engaged in fraud as a party to a securities transaction, or (2) engaged in fraud to induce plaintiff to purchase or sell securities. See 401 F.2d at 886 (Moore, J., dissenting).

The present case follows the decision of the Second Circuit in abandoning these requirements. However, in a concurring opinion in that case, Judge Friendly stated that "the April 12 press release would be the worst possible case for the award of damages" and that the consequences of imposing civil liability on a corporation in these circumstances were "frightening" (401 F.2d at 868, 866).

Judge Friendly's "worst possible case" has now come to pass.

B. The unrestricted liability for damages imposed by the court below is in conflict with the legislative history and policy of the securities laws.

Those sections of both the 1933 and 1934 Acts creating private causes of action were carefully drawn to accomplish two purposes: "the protection of the public [and] * * * the least possible interference to honest business." H.R. Rep. No. 85, 73d Cong., 1st Sess. 5 (1933). Thus, where private damage suits were specifically authorized under the securities laws, Congress carefully provided appropriate restrictions upon the right of action—privity, short statutes of limitation, *scienter,* causation and undertakings for costs (*e.g.,* 3 Loss, SECURITIES REGULATION 1765, 1778, *et seq.*)—so that honest businesmen, acting in good faith, would not be subject to threats of harassing lawsuits and enormous judgments.

The Tenth Circuit, however, in following cases under Section 12(2) of the 1933 Act (*e.g., Gilbert* v. *Nixon,* 429 F.2d 348 (10th Cir. 1970)) and concluding that the burden of proof on the *scienter* issue should be placed on defendants,* has disregarded Congressional limitations and has upset the balance between protecting the public, on the one hand, and responsible businessmen, on the other. Section 12(2)—which gives to a purchaser of securities a right to sue the seller—has several explicit restrictions built into the statute which are not present in Rule

* Such a result had never before been reached and is diametrically opposed to the prevailing rule in the Second Circuit. *Fischman* v. *Raytheon Mfg. Co.,* 188 F.2d 783 (2d Cir. 1951); *Shemtob* v. *Shearson, Hammill & Co., Inc.,* No. 71-1504 (2d Cir., August 31, 1971).

10b-5, such as the requirement that the defendant be the seller of securities and thus the person who profited from misstatements; a short statute of limitations, Section 13 of the 1933 Act, and provision for security for costs, Section 11(e). The privity requirement of Section 12(2) is particularly significant because the decision below holds Texas Gulf liable to sellers of its securities, even though Texas Gulf did not buy or sell securities and was not enriched in any degree.

In comparing civil liability under the 1933 and 1934 Acts, Professor Loss has remarked:

> "* * * the express civil liabilities under this Act (the 1934 Act) are much less rigorous than those under the 1933 Act—reflecting a watering down of the original draft in the light of the expressed fears that corporate managements would 'strike' against listing their securities on exchanges and putting their heads into the lion's mouth. * * *" 3 Loss, SECURITIES REGULATION 1746-1747 (1961).

The legislative scheme thus does not contemplate the imposition by implication of standards of responsibility under Section 10(b) and Rule 10b-5 which are far more strict than those imposed under the express provisions of the 1933 Act. In commenting on anomalous results similar to that reached by the court below, Loss states that this Court may be persuaded "to throw its collective hands *up* and the [implied private liability] doctrine out." 3 Loss, SECURITIES REGULATION 1790 (1961). No such action, however, is required to reverse the decision below; to restore some reason to the law, this Court need only hold that "fraud" means at least knowledgeable wrongdoing and that the requirement that the act complained of be "in con-

nection with the purchase or sale of securities'' means at least that the wrongdoing must be integrally related to a securities transaction. These common-sense propositions are what the statute and rule say, and they constituted the law prior to this and the *SEC* action.

In addition to the specific legislative history, the general policy behind the securities laws requires reversal of the result reached by the Tenth Circuit. Prior to initiation of its suit against Texas Gulf, the SEC referred to the ''commendable and growing recognition on the part of industry and the investment community of the importance of informing security holders and the public generally with respect to important business and financial developments.'' Securities Act Release No. 3844 (October 8, 1957). Such disclosure can hardly be promoted by a rule of law that voluntary, good faith, corporate statements not connected with securities transactions and issued only to warn the public against false and extravagant rumors will expose a company to damage suits from all claiming to have been misled thereby.

C. The standards enunciated by the Tenth Circuit, which ignore altogether the good faith judgment of Texas Gulf's management, place an impossible burden of compliance on corporations and will inhibit disclosure of business information.

Not only did the Tenth Circuit create a liability which did not exist before, but it formulated standards for press releases which are not intimated in the statute or rule. And, in giving these standards *ex post facto* application, it held that failure to comply with those newly devised

standards constituted "fraud." But Texas Gulf made no false statements, nor did it purport to set forth any statement at all as to what had been found by the drilling at Timmins. The release merely warned against accepting rumor as fact and promised a further statement "when reasonable and logical conclusions can be made." The good faith determination of Texas Gulf officials that such conclusions could not then be made was supported at trial by the testimony of four eminent mining experts.

However, the Tenth Circuit held that the release was insufficient and misleading as a matter of law; that Rule 10b-5 required Texas Gulf to set forth the drilling data it then had; *i.e.*, "to unveil the then known dimensions and drilling data of their discovery" (53a). Yet at the time Texas Gulf spoke, and indeed to this day, no rule or regulation of the SEC has ever required or even suggested that disclosure of preliminary drilling data should be made in documents filed with that agency. To the contrary, the whole thrust of enforcement under the securities laws has been to discourage disclosure of preliminary data. See, *e.g., Item 8A(b) of Schedule I to Form 1-A relating to Regulation A offerings under the Securities Act of 1933,* 1 CCH Fed. Sec. L. Rep. ¶7327 (77a).

The Tenth Circuit recognized that the honest opinion of the management of Texas Gulf, consisting of several mining engineers and geologists, was that at the time the release was issued, the available drilling data was not yet sufficient to reach responsible conclusions (44a); in those circumstances, it can hardly be "fraud" for management to conclude that the disclosure of such prelimi-

nary and inconclusive data was neither necessary nor desirable. The interpretation and application of Rule 10b-5 in this case goes beyond the authority granted by §10(b) of the 1934 Act.

The scrutiny of the press release by the Tenth Circuit was more appropriate to review of a registration statement or prospectus than a press release. Not only are the former documents prepared with painstaking care over long periods of time to conform with precise rules, regulations and schedules promulgated by the SEC, but they are also documents designed to elicit funds for the benefit of the issuer. Here the press release was drafted under great pressure on a weekend to respond to extravagant rumors in a situation where no guidelines existed; furthermore it was not designed to obtain any economic benefit for the corporation or its officers.

Moreover, Texas Gulf's right to comment upon matters of public interest to its shareholders is protected by the First Amendment. As discussed in the companion petition in the *SEC* action (No. 327, at pp. 27-30), imposition of liability upon Texas Gulf in these circumstances violates basic constitutional rights.

In sum, the effect of the present decision is that Texas Gulf, acting in good faith and without any ulterior purpose, has been judged in hindsight under newly-created, court-made rules which go beyond the statute and indeed contradict legal precedents and administrative practice under the securities laws, and having been so judged, is now required to account, perhaps to thousands of persons, for paper profits to which those persons have been encouraged to feel entitled.

II

The Tenth Circuit compounded the effect of its erroneous decision on the scope of Rule 10b-5 by permitting recovery by persons who sold after the issuance of a second release announcing a major ore discovery and by fashioning a rule of damages which requires innocent shareholders to pay large sums to those who have not been damaged.

Not only did the Tenth Circuit determine that Texas Gulf could be liable to all sellers of its stock because of its April 12 release, but it also concluded that such liability should extend to persons who sold after the promulgation and receipt in brokerage houses and elsewhere throughout the country of a second release announcing a major ore discovery. This result places an enormous burden on publicly-held companies which have thousands of shares traded on the exchanges every day, and ignores both the realities of the situation and case law.

The realities of the situation are clear. The information conveyed by the second release was in the hands of respondents' agents, their stock brokers, before respondents sold; in order to place their sell orders, respondents would have had to call their brokers and presumably would have learned of the second release. Whether they actually learned of that second release or not, notice of the April 16 release delivered to the brokers must be imputed to their customers. *Great American Indemnity Co.* v. *First Nat'l Bank*, 100 F.2d 763 (10th Cir. 1938); RESTATEMENT (SECOND) OF AGENCY, §272 (1957). If the agent fails to inform the principal in such circumstances, the principal is charged with the knowledge of his agent, the principal hav-

ing selected him and confided to him the business at hand. See *Schram* v. *Burt,* 111 F.2d 557, 563-64 (6th Cir. 1940).

Regardless of the question of imputation of the brokers' knowledge to the respondents, Texas Gulf cannot be held responsible for damages after the issuance of the April 16 press release. The issuance of a further statement by the same means by which the first statement was issued puts an end to any possible liability resulting from that first statement. *Vulcan Metals Co.* v. *Simmons Mfg. Co.,* 248 Fed. 853 (2d Cir.), *cert. denied,* 247 U.S. 507 (1918). Similarly, in *Shappirio* v. *Goldberg,* 192 U.S. 232 (1904), this Court held:

> "When the means of knowledge are open and at hand or furnished to the purchaser or his agent and no effort is made to prevent the party from using them, and especially where the purchaser undertakes examination for himself, he will not be heard to say that he has been deceived to his injury by the misrepresentations of the vendor." *Id.* at 241-242.

In *City Nat'l Bank* v. *Vanderboom,* 422 F. 2d 221, 231 (8th Cir.), *cert. denied,* 399 U.S. 905 (1970), the Court of Appeals quoted this language in denying recovery to a seller of stock in a §10(b) action.

The Tenth Circuit's refusal to apply these well-established principles has drastic consequences for a company whose stock is publicly traded. Despite its best efforts to clarify and explain, Texas Gulf can, under the Tenth Circuit's reasoning, be held liable to thousands of selling shareholders who will claim not to have gotten the word, despite its availability in every brokerage office.

Not only did the Court of Appeals permit respondents to recover on the basis of their sales made after dissemi-

nation of the second release, but it awarded damages to them based on the high price of the stock *two weeks* thereafter. In a rapidly rising market, this can mean the imposition of staggering liability on a publicly-held company, in reality, upon its shareholders. The rule has no support in precedent or reason.

Under the federal out-of-pocket rule, which has been held to govern the award of damages in the federal courts since *Smith* v. *Bolles,* 132 U.S. 125 (1889), damages are to be based on the difference between the sale price and the real or actual value at the time of sale. 3 Loss, SECURITIES REGULATION 1629 (1961). At the time of respondents' sales, the information in the April 16 release had been disclosed, and the sharp upward movement of the stock and the heavy trading confirmed that the information had affected the price of the stock. Indeed, before respondent Mitchell sold his stock on April 17, his brokers had stated in an investment letter that the price of the stock reflected the existence of 25,000,000 tons of ore disclosed in the April 16 release.

In any event, there can be no warrant for giving selling stockholders the benefits of increases taking place up to two weeks thereafter.* By that time, other factors, including Texas Gulf's annual meeting and further announcements by Texas Gulf as to the dimensions of the ore body, had intervened, and the price of the stock had increased. The Tenth Circuit justified its harsh rule of damages on the ground that "the wrongdoer is not heard to complain."

* The trial court based its damage award on the average of the high price over a period of one month. TGS stock sold at lower prices for the balance of the month after the date selected by the Court of Appeals. The Court may wish to take judicial notice of the fact that the stock is selling at a much lower price today (after accounting for a three-for-one split).

This rule has its origin and applicability to instances in which the "wrongdoer" profits from the wrong at the expense of the injured party. But the "wrongdoer" who is required to pay is the innocent Texas Gulf shareholder who did not think that the release was ground for selling, but was rather reason either to hold or to buy. Texas Gulf did not profit by issuing the press release. These respondents did not lose money upon their investments, and indeed received more for the stock than they paid for it. The "damages" awarded were additional speculative profits they might have made if they had held on to their stock and sold at some later optimum time. As Judge Friendly predicted, the rule of law enunciated by the Tenth Circuit will simply mean "large judgments, payable in the last analysis by innocent investors, for the benefit of speculators and their lawyers. * * *" 401 F.2d at 867. With such a possibility looming, a publicly held company is not likely to make a statement which is not legally required, but might well prefer to let the false rumors do their work.

III

The Tenth Circuit decision, in adopting a fraud statute of limitations in an action where there was no finding of fraud, conflicts with a well-reasoned decision of the Eighth Circuit.

Section 10(b) and Rule 10b-5 do not contain any statute of limitations. The right of action under that statute and rule has been implied by the judiciary, and the express statutes of limitation contained in the 1934 Act have not been applied. The federal courts have instead looked to the state limitations period for guidance. Several courts have in the past used the *fraud* provisions of the forum

state as the proper guide in framing a limitations period. Here the District Court held that the Utah three-year fraud statute applied, and the Court of Appeals affirmed.

However, as demonstrated above, the liability of petitioners herein was not predicated upon a finding of fraud, of which there was no evidence in the record; in these circumstances, the claim has become much more like a Blue Sky action than a fraud action. As Professor Loss has stated in his treatise, under the "most nearly analogous test", the statute of limitations period should be that found in the state Blue Sky laws. 6 Loss, SECURITIES REGULATION 3902 (1969). That was the result reached by the Eighth Circuit in *Vanderboom* v. *Sexton,* 422 F.2d 1233 (8th Cir.), *cert. denied,* 400 U.S. 852 (1970). The court there said that the Arkansas Blue Sky provision bore "the closest resemblance to the federal statute involved" and that it was "the most reasonable and logical type of statute to apply to which might be termed an 'implied federal blue sky' type of statutory action." 422 F. 2d at 1237-38. If the Utah Blue Sky provision were adopted,* providing for a two year statute of limitations, both respondent Reynolds and respondent Mitchell would be time-barred.

---

* The substantive provisions of Section 61-1-22(1)(b) of the Utah Code closely parallel Rule 10b-5(2):

> "(1) Any person who * * *
>
> "(b) offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading * * *."

Section 61-1-22(5) provides in relevant part that "[n]o person may sue under this section more than two years after the contract of sale."

IV

The decisions of the District and Circuit Courts, asserting jurisdiction over petitioner Fogarty, contravene constitutional principles enunciated by this Court.

The courts below have asserted personal jurisdiction over petitioner Fogarty, although there was no evidence that he had any contacts with the state in this matter. The constitutional principle set forth in *Hanson* v. *Denckla,* 357 U.S. 235, 253 (1958), makes it "essential in each case that there be some act by which the defendant purposefully avails itself of the privilege of conducting activities within the forum state, thus invoking the benefits and protections of its laws."

Here, the evidence demonstrated that Dr. Fogarty drafted the press release in his home in Rye, New York, as part of his duties with the corporation. TGS disseminated the release in New York, and reports of it were transmitted from there by the news media, including Dow-Jones, throughout the nation. TGS conducted potash mining activities in Utah and was properly "found" there. However, Dr. Fogarty as an individual was not "found" there and his activities, as above described, do not constitute "purposefully avail[ing] [him]self of the privilege of conducting activities within [Utah]." Thus the District Court's assertion of jurisdiction over him violated the constitutional principles set forth in *Hanson, supra.*

Conclusion

Rule 10b-5, as interpreted by the courts, has been allowed to supplant and upset the legislative scheme enacted by the Congress to balance the investors' need for protection and information with the legitimate requirements of responsible and honest business. The incongruity of an otherwise directed administrative rule supplanting Congressional direction is the product of a process by which the courts have, in case after case, extended Rule 10b-5 just one step further. Professor Loss has warned that "we can't go on indefinitely piling interpretation on interpretation on interpretation." 22 Bus. Law. 921 (1967). The final result, represented by the Tenth Circuit's opinion herein, is a structure built on the quicksand of faultily applied precedent, judicial legislation and misconstruction of the securities laws.

Only this Court can restore a sound foundation based on the provisions of the Rule in the context of the securities legislation enacted by Congress. Rule 10b-5 was promulgated by the SEC to aid its function of preventing fraud by purchasers of securities.* The proper construc-

* In its release announcing the adoption of Rule 10b-5, the Commission stated:

> "The Securities and Exchange Commission today announced the adoption of a rule prohibiting *fraud by any person in connection with the purchase of securities.* The previously existing rules against fraud in the purchase of securities applied only to brokers and dealers. The new rule closes a loophole in the protections against fraud administered by the Commission *by prohibiting individuals or companies from buying securities if they engage in fraud in their purchase.*" Securities Exchange Act Release No. 3230 (May 21, 1942). (Emphasis added.)

See also Freeman, 22 Bus. Lawyer 922 (1967).

tion of the Rule would preclude respondents here, and others with similar claims, from recovering from petitioners and the Texas Gulf shareholders, damages based on the good faith attempt by the company to clarify the status of its rapidly developing exploration at Timmins.

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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September 23, 1971

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Appendix A

Opinion of the District Court
(Dated January 9, 1970)

UNITED STATES DISTRICT COURT

DISTRICT OF UTAH, CENTRAL DIVISION

C-62-67

WALTER A. MITCHELL,

Plaintiff,

v.

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

Defendants.

C-132-66

GEORGE GORDON REYNOLDS,

Plaintiff,

v.

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

Defendants.

C-54-67

ARTHUR R. STOUT, JR., and MARY LOUISE STOUT, Wife,

Plaintiffs,

v.

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

Defendants.

Appendix A—Opinion of the District Court

RITTER, C. J.

Common to all four cases, which were consolidated for trial, are alleged violations of Sec. 10(b) of the Securities and Exchange Act of 1934[1] and Rule 10b-5 promulgated by the Securities and Exchange Commission.[2] One complaint includes a count in common law fraud, another alleges a conspiracy between the defendants to violate Sec. 10(b) and Rule 10b-5. Another complaint alleges violations by defendants of affirmative fiduciary duties to disclose inside information, and alleges violations of Sec. 9 of the Securities and Exchange Act of 1934.[3] The cases have been tried upon the theory of violations of Sec. 10(b) and Rule 10b-5. The other claims have not been pressed. Recovery of damages under the theory of violations of Sec. 10(b) and Rule 10b-5 precludes recovery of further damages in any event.

After the actions were filed, defendants filed an original action with the United States Court of Appeals for the Tenth Circuit under its Rule 28, seeking a writ of prohibition to restrain the trial judge from proceeding to try the actions, and a writ of mandamus directing the trial judge to (a) set aside his order denying petitioners' motion to transfer the cases to the United States District Court for the Southern District of New York under 28 U.S.C. Sec. 1404 (a), (b) transfer the cases as to defendant Texas Gulf Sulphur Co., and (c) either dismiss the action as to defendant Charles F. Fogarty or, in the alternative, transfer the case as to such defendant to the New York Federal Court.[4] The Court of Appeals, without making any final

1. 15 U.S.C. Sec. 78j(b).

2. 17 C.F.R. 240.10b-5.

3. 15 U.S.C. Sec. 78i.

4. Texas Gulf Sulphur, et al. v. The Honorable Willis W. Ritter, et al., 371 F.2d 145 (1967).

determination of facts necessary to prove venue, refused to issue either a writ of prohibition or a writ of mandamus, and upheld the action of the trial judge in overruling the motion attacking venue. The court stated that as to the corporate defendant venue and process are good "because, without dispute, it transacts business in Utah." As to both the individual defendant, Fogarty, and the company, the court held venue will lie in the Utah district "if any of the acts or transactions complained of took place in that district" and, further, that if "venue lies in Utah for that reason, valid process may be had upon Fogarty personally 'in any other district of which the defendant is an inhabitant or wherever the defendant may be found.'" Fogarty's preparation and issuance of a press release to representatives of financial firms and newspapers for transmission over instrumentalities of interstate commerce to branch offices and newspapers throughout the country, which press release plaintiffs contend violated Sec. 10(b) and Rule 10b-5, is sufficient to satisfy requirements of venue and service of process as to defendant Fogarty in three of the four actions. Defendants contend that as to the fourth action there is no venue or proper service of process on Fogarty because the plaintiff in that action sold his stock in December, 1963, several months before issuance of the press release, and because none of the acts or transactions complained of took place in the Utah District.

JURISDICTION

Jurisdiction as to all parties exists (a) under 28 U.S.C. Sec. 1331, the amount in controversy in each of the consolidated cases being in excess of $10,000.00, exclusive of interest and costs, and there being necessary diversity of citizenship between the parties in each case, and (b) by virtue of the allegations in each case of violations of provisions of Sec. 10(b) of the federal statute and S.E.C. Rule 10b-5.

Appendix A—Opinion of the District Court

FACTUAL BACKGROUND

In November, 1963, Texas Gulf Sulphur Co. (herein sometimes "TGS") core drilled an anomaly[5] near Timmins, Ontario, Canada, which had been detected during the course of an aerial and ground geophysical survey program. The drilling of this hole[6] was completed November 12, 1963, at a depth of 655 feet. Visual examination of the core by the company's chief geologist, Walter Holyk, indicated an average copper content of 1.15%, and an average zinc content of 8.64% over a length of 599 feet. The core was split longitudinally and one-half was sent to a Utah assay house for chemical analysis. The chemical assay proved that the visual appraisal was uncommonly accurate. It disclosed an average mineral content of 1.18% copper, 8.2% zinc, and 3.94 ounces of silver per ton over a length of 602 feet.

The visual appraisal of the core prompted the company to take steps to improve its position without waiting for the chemical assay. The anomaly tested by this hole included lands to which the company did not at the time have the mineral rights, and TGS concluded that additional tracts of adjoining land should be acquired. Immediate action was taken to maintain secrecy as to the results of the first hole. The president of the company issued an order that no one outside of the exploration group[7] should be told of the prospect, the drill camp was moved to another site, all signs of drilling activity were removed and the drill site was camouflaged by standing cut saplings in the snow.

5. An area where there are variations in electrical conductivity, from normal background, of underlying rock formations.

6. The initial hole was on what was known as the Kidd-55 segment of land. It was designated K-55-1. Subsequent holes were designated K-55-2, K-55-3, etc.

7. The information was even withheld from other officers, directors and employees of TGS.

A second hole was intentionally drilled off of the anomaly to divert attention from Kidd-55-1, and the barren core was left lying on the ground near K-55-2.

The importance of the findings based on the core from the first test hole was indicated by a Memorandum for the Files, prepared November 14, 1963, by the company's chief geologist, in which the statement was made that this drill hole "intersected significant copper and zinc mineralization throughout the entire cored length of 655 feet." The author of the memorandum noted that the intersection was "obviously of ore grade" but he warned against "extrapolating this intersection to tonnage estimates" and pointed out that it would be impossible to estimate the true width of the sulphide zone until a second drill hole was directed across the intersection from west to east. The first hole had been drilled from east to west. He concluded the memorandum with the observation that efforts should be made to acquire adjoining lands through purchase or option agreements.

TGS acquired three additional 160-acre tracts adjacent to the site of the initial drill hole—one in December, 1963, another in February, 1964, and the third on March 27, 1964.[8] Drilling was resumed on March 31, 1964, when drill hole K-55-3 (in reality the *second test hole* because K-55-2 was intentionally drilled off of the anomaly) was commenced. It was started 510 feet west of K-55-1 and was drilled in an easterly direction at a 45 degree angle so as to cross

8. Defendant's Exhibit P-2 includes photostat copy of a story that appeared in the April 17, 1964 issue of the Wall Street Journal relative to the press conference held April 16, 1964, at which TGS announced its "major strike". The story quotes Claude O. Stephens, president of TGS, as stating that Texas Gulf's "land position is favorable" and further that "Texas Gulf holds the mineral rights in 70% of Kidd township and has substantial acreage in adjacent townships." The Wall Street Journal story also reported that another TGS official had estimated that TGS had options, claims or ownership of about 60,000 acres in the area.

K-55-1 in a vertical plane. It was completed by 7:00 p.m. April 7, 1964.[9] Visual appraisal of the core of K-55-3 compared very favorably with both the visual appraisal and the chemical assay of the core of the first drill hole. The visual examination of the third core indicated an average mineral content of 1.12% copper and 7.93% zinc over 641½ feet of its 876-foot length. This core eliminated the chance that K-55-1 had been drilled "down-dip" and established generally the east and west margins of the sulphide ore body.

Test hole K-55-4 was started 200 feet *south* of K-55-1 and was drilled from east to west at a 45 degree angle in a vertical plane parallel to the vertical plane of the first hole. It was completed by 7:00 p.m., April 10. Again, visual examination of the core indicated significant mineralization—mineral content of 1.14% copper and 8.24% zinc for 366 feet of its 579-foot length. The significance of the date and time—April 10, 7:00 p.m.—lies, first, in the admission by defendants that although its press release of Sunday, April 12, purported to reflect the results of drilling "done to date" it actually was based upon drilling information as of the evening of April 10, and, second, in the contention of plaintiffs that even upon the basis of information available on the evening of April 10, the press release was inaccurate and misleading.

By 7:00 p.m. on April 10 some drilling had been done in holes K-55-5 and K-55-6. K-55-5 was started on April 10 at a point 200 feet *north* of K-55-1, and was slanted westerly at an angle of 45 degrees in a vertical plane parallel to an assumed plane containing K-55-1 and K-55-3. At 7:00 p.m. that evening substantial copper mineralization had been encountered over the last 42 feet of this hole's length

9. Because of the importance of events occurring between March 31 and April 16, 1964, particular dates and times are of special significance.

at that time, which was 97 feet. K-55-6 was started on April 8, two days before the start of K-55-5, at a point 300 feet *easterly* of K-55-1. It was drilled in a westerly direction at an angle of 60 degrees, and was intended to explore mineralization *beneath* K-55-1. By the evening of April 10, substantial copper mineralization had been encountered over the last 127 feet of the hole's length, which at that time was 569 feet.

Between the evening of April 10 and the morning of April 13, when the press release information was published substantial copper mineralization had been encountered in K-55-5 to the 580-foot mark, an additional 483 feet of mineralization since the evening of April 10, and visual estimates of the core indicated an average mineral content of 0.82% copper and 4.2% zinc over a 525-foot length. At that time K-55-6 had been drilled to the 946 mark and had encountered mineralization. Two more holes, K-55-7 and K-55-8, were commenced on April 12 and 11, respectively. K-55-8 was a broader hole drilled for the purpose of obtaining a core that could be used in metallurgical tests of the amenability to milling of the materials encountered.

Rumors in Canada and New York

Although the company had treated the first test hole as "tight", rumors began to spread shortly after the first of the year 1964, and there was considerable excitement in Timmins and Toronto about a reported discovery. By early April, 1964, there was a "tremendous staking rush going on", according to the testimony of Richard D. Mollison, TGS vice president in charge of exploration, and lands within several miles of the area had been staked. People were watching all surface traffic, and low-flying planes passed over the area several times a day. Silence and secrecy on the part of TGS and its officials were not effective to curb widespread rumors and speculation in Canada and later in New York.

Appendix A—Opinion of the District Court

On April 9, 1964, the Toronto Globe and Mail published a story in which it was stated that "Rumors that one of the biggest copper deposits in North America has been discovered near Timmins have Bar Street agog", and that in the past two weeks the Toronto Stock Exchange "has been experiencing its wildest speculative spree since the Nineteen Fifties." The Toronto Daily Star on the same day stated that rumors had gained ground "of a major copper strike about 10 miles North of Timmins by Texas Gulf Sulphur Co." On April 10 the Toronto Globe and Mail reported that speculative mining fever still gripped the Toronto stock market "as officials of Texas Gulf Sulphur Co. of New York maintained a tight-lipped silence on what —if anything—they have discovered in Northern Ontario."

The rumors spread to the United States and on the morning of Saturday, April 11, 1964, both the New York Times and the New York Herald Tribune carried stories about the rumored discovery. The Times story referred to an unverified rumor that TGS "had made a sensational copper strike" that had caused "feverish activity in penny speculatives on the Toronto market," and to a reported surge of staking in various townships flanking Timmins, and to hotels and motels bulging with prospectors and would-be prospectors. The story in the Herald Tribune in part reported:

> The biggest ore strike since gold was discovered more than 60 years ago in Canada has stampeded speculators to the snowbound old mining city of Timmins, Ontario, some 450 miles northwest of Toronto.
>
> This time it's copper * * *
>
> The story of the strike goes something like this: Texas Gulf Sulphur has been active in the Big Water area, accessible only by airplane, for several years. The richness of the copper it discovered was so great

that samples reportedly were flown out of the country to be assayed.

The huge lode is supposed to consist of a bed of copper sulfite (sic) 600 feet wide with a possible overall copper return of 2.87 per cent through most of its width. This yield, in itself, is considered rich in mining circles.

But the richest yield comes from the first 100 feet of that 600-foot belt. It is supposed to be 5.6 per cent, a bonanza if the story proves more than just a myth. But myth it may be * * *

The story of the strike reportedly leaked out when it was discovered that certain employees of Texas Gulf Sulphur were buying into the company's stock * * *

Press Release of April 12

With the appearance of the Times and Herald Tribune stories TGS decided to issue a press release. The president of the company, Claude O. Stephens, directed the executive vice president, Charles F. Fogarty, to prepare the release. After consulting with public relations advisers, legal counsel, the vice president in charge of exploration, and others, the following statement (quoted in pertinent part) was given to newsmen and representatives of financial publications in the late afternoon or early evening of April 12:

"New York, April 12—The following statement was made today by Dr. Charles F. Fogarty, Executive Vice President of Texas Gulf Sulphur Company, in regard to the company's drilling operations near Timmins, Ontario, Canada. Dr. Fogarty said:

" 'During the past few days, the exploration activities of Texas Gulf Sulphur in the area of Timmins, Ontario, have been widely reported in the press, coupled with rumors of a substantial copper discovery

there. These reports exaggerate the scale of the operations, and mention plans and statistics of size and grade of ore that are without factual basis and have evidently originated by speculation of people not connected with TGS.

" 'The facts are as follows. TGS has been exploring in the Timmins area for six years as part of its overall search in Canada and elsewhere for various minerals—lead, copper, zinc, etc. During the course of this work, in Timmins as well as in Eastern Canada, TGS has conducted exploration entirely on its own, without the participation of others.

" 'Numerous prospects have been investigated by geophysical means and a large number of selected ones have been core-drilled. These cores are sent to the United States for assay and detailed examination as a matter of routine and on advice of expert Canadian legal counsel. No inference as to grade can be drawn from this procedure.

" 'Most of the areas drilled in Eastern Canada have revealed either barren pyrite or graphite without value; a few have resulted in discoveries of small or marginal sulphide ore bodies.

" 'Recent drilling on one property near Timmins has led to preliminary indications that more drilling would be required for proper evaluation of this prospect. The drilling done to date has not been conclusive, but the statements made by many outside quarters are unreliable and include information and figures that are not available to TGS.

" 'The work done to date has not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly mis-

leading. When we have progressed to the point where reasonable and logical conclusions can be made, TGS will issue a definite statement to its stockholders and to the public in order to clarify the Timmins project * * *." "

Plaintiffs contend that the foregoing press release is inaccurate, incomplete, misleading and deceptive. Defendants take the position that it was accurate at the time it was prepared and issued. Before discussing the contentions of the parties with respect to the press release we call attention to a few more facts.

Public Announcements of Major Strike on April 16

On the day that the information contained in the foregoing press release was published—Monday, April 13—a reporter for The Northern Miner, a Canadian mining industry journal, by invitation visited the properties near Timmins, inspected the drill cores and conferred with TGS officials, including its chief geologist and its vice president in charge of exploration. Around the first of April, approximately 12 days prior to the press release, Mr. G. M. Ackerley, a reporter with The Northern Miner, had been orally invited by a vice president of TGS to visit the properties on April 20, 1964, for the purpose of preparing an article. This oral invitation was confirmed by a letter dated April 6 from vice president Richard D. Mollison, who testified that he gave Ackerley the invitation in response to repeated requests from him "and because of all the wild rumors and wild statements that were already so prominent in that district, and with my expectation that three weeks' time, three weeks of drilling, would throw some light on what there was and he could come up then at the end of that three weeks and see what it was." A meeting of the stockholders of TGS had been scheduled

for April 23. Mr. Mollison further testified that because of the development of the rumors in Canada and New York they decided to invite Mr. Ackerley to come a week earlier.

On the basis of what he saw and heard on April 13, Mr. Ackerley prepared an article which, in accordance with previous understanding, he submitted to Mr. Mollison for him to hold until the company was ready to release the same. Mr. Mollison made an insignificant change by adding some names of exploration department personnel and on April 15 returned the article to Mr. Ackerley for publication. It was published on the morning of April 16, the same day that TGS notified the press in New York that it had made a major strike. In pertinent part Mr. Ackerley's article read:

> "Texas Gulf Sulphur has chalked up a brilliant exploration success * * * a major new zinc-copper-silver mine is definitely in the making * * *
>
> "* * * on the basis of seven tests either completed or drilling it can be stated that a strike length of 600 ft. minimum has been established showing an ore width of roughly 300 ft. which has been traced so far to a maximum vertical depth of about 800 ft. * * * this must be recorded as one of the most impressive drill holes completed in modern times.
>
> "For a core length of a shade better than 600 ft., the hole averaged in excess of 1% copper, 8% zinc and nearly four ounces of silver.
>
> "And there are impressive, strong sections within this width which in themselves are quite spectacular. In the upper part of the hole, for example, a core length of 82 ft. ran 7.1% copper, 9.7% zinc, and 2.4 ozs. silver. And still deeper, a strong zinc section of better than 100 ft. averaged out to in excess of seven ounces of silver in addition to ore-grade zinc values * * *

"From the dimensions already known, the Northern Miner can say that something in excess of 10,000,000 tons of ore is indicated. It is capped with something like 20 ft. of overburden, presenting no stripping problems, and the steep dip and wide widths will lend themselves ideally to an open-pit mining situation.

"The picture should unfold rapidly at this stage, but officials emphasize that it is still at the embryo point * * *"

On April 16, TGS announced to the press a strike of at least 25,000,000 tons of ore. A prepared release was read to representatives of the press and of financial publications at 10:00 A.M., and summaries of the announcement appeared on the private wire services of Merrill, Lynch, Pierce, Fenner and Smith and of Dow Jones within the hour. In part this release read:

"Texas Gulf Sulphur Company has made a major strike of zinc, copper and silver in the Timmins area of Ontario, Canada. * * *

"Seven drill holes are now essentially complete and indicate an ore body of at least 800 feet in length, 300 feet in width and having a vertical depth of more than 800 feet * * *

"This is a major discovery. The preliminary data indicate a reserve of more than 25 million tons of ore. The only hole assayed so far represents over 600 feet of ore, indicating a true ore thickness of nearly 400 feet * * *

"Visual examination of cores from the other holes indicates comparable grade and continuity of ore.

"The ore body is shallow having only 20 feet of over-burden. This means that it can easily be mined initially by the open-pit method * * *"

Appendix A—Opinion of the District Court

Stock Purchases and Stock Option Acquired by Fogarty

The record establishes that prior to completion of the first test hole on November 12, 1963, Fogarty had purchased a total of 705 shares of TGS stock. On that date he purchased 300 shares, on November 15, 700 shares, on November 19, 500 shares and on November 26, an additional 200 shares. On December 30 and 31, 1963, which was about two weeks after the company received the chemical assay reports on the core taken from the first hole, Fogarty purchased 300 shares. Drilling was resumed on March 31, 1964, and the following day Fogarty bought 400 shares of TGS stock, and an additional 300 shares on April 6, making a total of 3100 shares of TGS stock purchased between November 12, 1963, and April 6, 1964.

On February 20, 1964, Fogarty received a stock option for 7300 shares of TGS stock. Other TGS officials also accepted stock options on that date. The evidence establishes that members of the stock option committee were not aware of the results of drilling near Timmins at the time the stock options were awarded. Fogarty subsequently surrendered his stock option unexercised, and "returned" to the company at his cost all stock purchased by him during the period November 12, 1963 to April 6, 1964. The record discloses that other TGS officials, including Richard D. Mollison, vice president in charge of exploration, and the company's chief geologist, Walter Holyk, either personally or through agents purchased TGS stock during the same period, as did several other employees of the company.[10] All purchases of TGS stock by Fogarty were made through the New York stock exchange.

10. Some of the purchases were of "calls" for TGS stock. A "call" is a negotiable option contract by which the bearer has the right to buy from the writer of the contract a certain number of shares of a particular stock at a fixed price on or before a certain agreed-upon date.

Purchases and Sales of TGS Stock by Plaintiffs

Plaintiffs purchased and sold stock in Texas Gulf Sulphur Company as follows:

George Gordon Reynolds: purchased 300 shares January 7, 1960, at $18⅝ per share, and 200 shares on May 18, 1962, at $15 per share. He sold 500 shares on April 16, 1964, at $33⅝ per share.

Arthur R. Stout and wife: purchased 1,000 shares February 5, 1962 for $20½ per share. They sold 1,000 shares April 21, 1964, at $42 per share.

Lawrence L. Karlson and wife: purchased 100 shares on October 10, 1963, for $16⅝ per share, and sold the same on December 11, 1963, for $20⅞ per share.

Walter A. Mitchell: purchased 420 shares between December 11, 1953, and May 17, 1962, at prices ranging from $15 to $80¼ per share. He sold 400 shares on April 17, 1964, for $40 per share, and 20 shares on April 23, 1964, for $46¼ per share.

VIOLATIONS OF SECTION 10(B) AND RULE 10B-5

Common to the complaints in all four cases are alleged violations of Section 10(b) of the Securities and Exchange Act of 1934,[11] and Securities and Exchange Commission Rule 10b-5.[12] The statutory provision in part provides:

"Sec. 78j. *Manipulative and deceptive devices.*

"It shall be unlawful for any person directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

11. 15 U.S.C. Section 78j(b).

12. 17 C.F.R. 240.10b-5.

"(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

The S.E.C. Rule, which is patterned in form and language after Section 17(a) of the Securities Act of 1933,[13] provides:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person."

Neither the statute nor the Rule expressly provides for private civil remedies for fraud or misrepresentation in Reynolds, et al, vs. Texas Gulf Sulphur Company, et al connection with a purchase or sale of any security, manipulative or deceptive practices, or for failing to disclose material information not otherwise available to the other

13. 15 U.S.C. 77q.

party to a transaction. Judicial decisions, however, have firmly established such civil remedies as being implicit in the provisions. A leading case, *Kardon* v. *National Gypsum Co.*[14] has been cited and followed in a number of later cases. In *Hooper* v. *Mountain States Securities Corp.*, the court said:

> "We need not repeat here the history now so well catalogued which traces the exercise by the SEC of the legislative power granted in Sec. 10(b) to promulgate regulation X-10B-5. A significant purpose of X-10B-5 was to extend to *sellers* the same protection against fraudulent and other unlawful schemes afforded to those defrauded in the purchase of securities. In a substantive way it is even more sweeping. It greatly expands the protection frequently so hemmed in by the traditional concepts of common law misrepresentation and deceit, the requirement of privity, proof of specific damage, inadequacy of the right of recission or right to recover up to par value of stock of a much greater market value. To these difficulties would have to be added the geographic obstacle of suit in a common forum against multi-state defendants scattered as far as the fraudulent device required * * *"

In the case of *Speed* v. *Transamerica Corp.*, supra, the court held that an implied misrepresentation can be just as fraudulent as an express one, that the three sub-paragraphs of Rule 10b-5 are mutually supporting and not mu-

14. 73 F.Supp. 798 (E.D. Pa. 1947). See also Fischman v. Ratheon Mfg. Co., 188 F.2d 783 (2d Cir. 1951); Speed v. Transamerica Corp., 99 F.Supp. 808; Hooper v. Mountain States Securities Corp., 282 F.2d 195 (5th Cir. 1960), cert. den. 365 U.S. 814 (1961); Slavin v. Germantown Fire Ins. Co., 174 F.2d 799 (3rd Cir. 1949); Fratt v. Robinson, 203 F.2d 627 (9th Cir. 1962); Stevens v. Vowell, 343 F.2d 374 (10th Cir. 1965); Kohler v. Kohler, 208 F.Supp. 808 (E.D. Wis. 1962), aff'd 319 F.2d 634 (7th Cir. 1963).

tually exclusive, and that a defendant's breach of duty to disclose accordingly can be viewed as a violation of all three sub-paragraphs, i.e., (1) a device, scheme, or artifice to defraud, (2) an implied misrepresentation or misleading omission, and (3) an act, practice or course of business which operates or would operate as a fraud.

Plaintiffs here contend that they have been damaged by violations of the statute and the rule by both the corporation and Fogarty, its executive vice president, (1) for failure to disclose prior to April 16, 1964, information as to the results of drilling at the property, and (2) in issuing an inaccurate, misleading and deceptive press release, which was published April 13, 1964. The decision to maintain secrecy and to not disclose the results of the drilling was made or concurred in by the president of the company, Claude O. Stephens, the executive vice president, Charles F. Fogarty, the vice president in charge of exploration, Richard D. Mollison, the company's chief geologist, Walter Holyk, and some other company officials and employees. Obviously, this was a decision of the corporation itself, even though some officers and directors were not informed of the drilling results until a public announcement was made on April 16, 1964.

Karlson Case

Plaintiff Karlson sold his stock on December 11, 1963, through a stock exchange. There was no face-to-face transaction. Fogarty did not purchase the particular shares sold by Karlson. While it is not necessary for Karlson to establish privity of contract in order to recover for violations of the statute or rule,[15] and the fact that there was a total non-disclosure would not prevent recovery if some

15. Cochran v. Channing Corp., 211 F.Supp. 239 (S.D. N.Y. 1962); Fischman v. Ratheon Mfg. Co., 188 F.2d 783 (2d Cir. 1951).

form of manipulation was involved,[16] it nevertheless is necessary for Karlson to prove some causative effect.

In the case brought against Texas Gulf Sulphur Company, Fogarty and other TGS officials and employees, by the Securities and Exchange Commission,[17] the Circuit Court found that Fogarty had violated Section 10(b) and Rule 10b-5 by purchasing TGS stock without publicly disclosing the insider information he possessed. It does not follow that such purchases by Fogarty, some of which were made prior to the time Karlson sold his stock, caused any damage to Karlson, and the record before us does not support any such contention. Corporations and their executives undoubtedly owe duties to stockholders to keep them reasonably informed as to corporate affairs and such matters as the mineral discovery here involved, but that duty does not surpass all other duties owed to stockholders. Here, for instance, the company and Fogarty were also under a duty to TGS stockholders, including Plaintiff Karlson, to not make information concerning the mineral discovery public until the company could first protect itself by acquiring mineral interests in adjoining lands. Plaintiff Karlson sold his TGS stock barely a month after completion of the first test hole and before the company had received all of the reports of the chemical analysis of the core extracted from that hole. The record discloses that such reports were received during the period December 9 to 13. He also sold prior to the time the company had been able to acquire the adjoining lands upon which the anomaly was found. The court believes it is not necessary to pass upon the materiality[18] of the information available to defendants on December 11, 1963, because of his findings

16. List v. Fashion Park, Inc., 340 F.2d 457 (2d Cir. 1965), cert. den. 382 U.S. 811 (1965).

17. Securities and Exchange Commission v. Texas Gulf Sulphur, et al., 401 F.2d 833, 842 (adv. sheets) (2d Cir. 1968).

18. See sub-paragraph (2) of Rule 10b-5, supra.

that there was no duty at that time on the part of either defendant to disclose the information then available with respect to drilling results, and that Fogarty's violations of the statute and the rule by purchasing TGS stock did not cause any damage to Plaintiff Karlson. The press release which the court has found to be misleading and inaccurate was not issued until four months after Karlson sold his stock.

Reynolds Case

Plaintiff Reynolds made two purchases of TGS stock, 300 shares on January 7, 1960, at $18⅝ a share, and 200 shares on May 18, 1962, at $15 per share. He sold his 500 shares early on the morning of April 16, 1964, after hearing about a "rumor" and a "flurry" in the stock, but before he learned that there had been an announcement of a "major strike" or "discovery." He testified that he sold on the strength of the April 12, 1964 press release, a summary of which came over the wires on the morning of April 13th.

An account executive with the Salt Lake City office of a national brokerage firm testified that after he read the summary of the April 12 release he telephoned Reynolds because he knew Reynolds was vitally concerned about TGS stock; that during their conversation he told Reynolds that the report "didn't make any positive statements about what had happened" and "that the report * * * didn't seem to substantiate the price action of the stock to that point." Reynolds testified that on the 13th he decided to hold the stock to see what happened, that he believed the press release, but that it made him feel that "someone was throwing a wet blanket" and that they were trying to say "we haven't got it."

Reynolds further testified that on April 16 the same account executive called him and "said there was a rumor

that Texas Gulf Sulphur had made a strike"; that he (Reynolds) "hardly believed it" but "thought it was a promotion propaganda of some kind" and decided to "get out while the getting was good." He sold his stock through the broker for $33⅝ per share. He also testified that if it hadn't been for the release which came over the wires on the 13th he would have kept his TGS stock; that if he had known of the November, 1963, test core hole he would have doubled his holdings. He did not learn of the contents of the April 16 release until later in the afternoon of that day (April 16) when the stock closed around $37, and that he did not buy back because "very few investors will ever chase a stock" and because he had already sold and was in a position where he would have to pay taxes on his profits.

From the record the court concludes that the press release dated April 12, 1964, was inaccurate, misleading and deceptive with respect to material matters disclosed by the company's drilling near Timmins. The authors of the release knew from visual and chemical analyses that the first core disclosed the presence of copper and zinc mineralization of ore-grade;[19] that the second test hole (K-55-3) virtually eliminated any chance that the initial test hole had been drilled "down-dip"; that cores from drill holes located 200 feet south and 200 feet north of the initial test hole contained similar mineralization; and that still another drill hole core had disclosed similar mineral-

19. In the Memorandum for the Files, previously referred to, prepared on November 14, 1963, by Chief Geologist Holyk, he wrote that the intersection encountered in the first drill hole was "obviously of ore grade." An article in the April 24, 1964 issue of the Wall Street Journal (part of defendant's Exhibit P-2) states that at the annual meeting of TGS stockholders held April 23, 1964 at Houston, the president of TGS in responding to questions from stockholders stated that "When we drilled the first hole, we knew we had something. But Canadian newspapers were carrying reports with no basis whatsoever."

ization at greater depths than were reached by the other drill holes.

The release painted a bleak and gloomy picture—most of the areas drilled in Eastern Canada revealed either barren pyrite or graphite without value; a few resulted in discoveries of small or marginal sulphide ore bodies, etc. Not a word, however, about the results of any of the drilling near Timmins, except that it had led to "preliminary indications" that more drilling would be necessary for a proper evaluation. The drilling "to date had not been conclusive" and has not been "sufficient to reach definite conclusions" and "any" statement "as to size and grade of ore would be premature and possibly misleading." But a newspaper reporter's finding, made on the same day the press release was printed, that the drillings indicated more than 10,000,000 tons of ore, and the same reporter's statement that one hole averaged in excess of 1% copper and 8% zinc, went unchallenged when submitted to vice president Richard D. Mollison who released the article on April 15th for publication. Obviously, the reporter was quoting figures given to him by officials of the company, and given to him on April 13th. It may very well have been that the company officials when they prepared the release dated April 12, were trying to hold the big news until just before, or on the day of, the stockholders annual meeting which was held on April 23rd. In any event, the court finds the release dated April 12 was deceptive, misleading and inaccurate and violated both the statutory section 10(b) and the Rule provision 10b-5, and finds that plaintiff Reynolds was misled and deceived to his detriment, and is entitled to recover damages.

With respect to Mr. Ackerley's statement that from his examination on the 13th of April there were in excess of 10,000,000 tons of ore indicated, it is interesting to note the testimony of one of plaintiffs' witnesses, Dr. Francis

W. Christiansen, a geologist. Dr. Christiansen testified that from his examination of cores, assays, logs and other data pertaining to drilling up to 7:00 p.m. on April 10, he calculated the indicated tonnage of ore at 7,390,000 tons. He testified further that drilling up to 7:00 p.m. on April 11, added 2,600,000 tons of indicated ore, and that drilling up to the evening of April 12 added 1,800,000 tons more, making a total 11,790,000 tons of indicated ore as of Sunday evening, April 12th.

Mitchell Case

Plaintiff Mitchell, a C.P.A., residing in Los Angeles, purchased 420 shares of TGS stock between December 11, 1953 and May 17, 1962, at prices from $15 to $80¼ per share. On April 16, 1964, the first free day he had had following the income tax season, he stopped by to see one of his brokers between 9:00 and 9:30 a.m., to inquire about TGS stock which he had noticed had been rising over several weeks. His broker gave him a copy of the "New York Morning News Digest", dated April 13, 1964, published by E. F. Hutton & Company, in which appeared the following:

> "In the financial press this morning, management of Texas Gulf Sulphur states that reports that it has discovered a large lode of rich copper in Canada are premature and possibly misleading."

He also read the article in the western edition of the Wall Street Journal for April 13, 1964, the first paragraph of which read:

> "New York—Texas Gulf Sulphur Co. called reports that it has discovered a large lode of rich copper ore in Canada 'premature and possibly misleading.' "

After reading the foregoing articles Mr. Mitchell returned to his office, reviewed his file on TGS and "came to the conclusion, based upon the report, the release of April

13 by Texas Gulf Sulphur, that the stock could not sustain its present rise and that it would fall back as soon as that release had been disseminated and recognition given to it by the public." He then went to a second broker and instructed him to sell 400 shares. It was a "short sale against the box." This was about 11:30 or 11:45 a.m. Later in the afternoon he discovered he had overlooked 20 shares and when he took the certificates for the 400 shares in to his broker he told the clerk that he would bring in the 20 shares the following morning and that they were to be sold. They were delivered on the morning of the 17th with instructions to sell short against the box.

At the time Mitchell sold his stock he had no knowledge of any press release other than that of April 12th. Under cross-examination he testified that "the reason I sold short was that I did not want to part with my Texas Gulf Sulphur stock. I reasoned that inasmuch as the market could not sustain itself in view of the report—the release of April 13—that I could sell short, buy back at a lower price, and in the meantime retain the stock I owned; namely, the 420 shares * * *"[20] On the 16th the bid price was in the neighborhood of $37 so he sold 400 shares at $40 a share. When he took the 20 shares in on the 17th the stock had gone up somewhat and he put those shares in at $45. Even though he gave his broker instructions to sell the 20 shares on the 17th, for some reason unknown to plaintiff Mitchell, the

20. A "short sale" is defined as follows in Patton's Accountant's Handbook (3rd Ed.): "A short sale is a transaction in which a trader in securities 'sells' a block of stock at the current price without making immediate delivery. Such a sale is made in anticipation of a decline in the price of the security; the trader expects to make a profit by buying the stock—'covering'—at a lower price. The postponing of delivery by the vendor is made possible through an arrangement by which the broker 'borrows' the stock for delivery to the party to whom the sale was made. Under the usual plan the trader is not required to cover as long as his account with the broker is properly protected."

order to sell was not put through by the broker until April 22, and the stock was sold on the 23rd for $46¼ per share.

Plaintiff Mitchell testified that the article in the Wall Street Journal of April 13 "was the motivation that caused me to sell short."

The court agrees with Plaintiff Mitchell that the press release dated April 12, 1964, was false, misleading, deceptive and fraudulent; that it contained misstatements of material facts and omitted and concealed material facts with respect to the progress of drilling—all in violation of Section 10(b) of the Securities Exchange Act of 1934, and S.E.C. Rule 10b-5. It omitted all information as to the results of chemical and visual appraisals of cores, and gave no information as to the number of holes drilled or the type of mineralization encountered. It was a misstatement to say that recent drilling had led to "preliminary indications that more drilling would be required for proper evaluations of this prospect" and it was deceptive to state that "work done to date has not been sufficient to reach definite conclusions and *any* statement as to size and grade of ore would be premature and possibly misleading" (emphasis added). The tenor of the entire statement was misleading, and, the court thinks designedly so.

Stout Case

Arthur R. Stout, Jr. and his wife owned 1,000 shares of TGS stock in joint tenancy, which had been purchased on February 5, 1962, at $21½ a share. Their order to sell was placed April 21, 1964, and the stock was sold the following day at $42 per share. Mr. Stout testified that the sale of the stock was motivated by information concerning the press release of April 12, 1964, which he received "probably within a week of the 13th." He had no recollection as to how he received the information, but from what he heard he "concluded that the officers of Texas Gulf

Sulphur had stated that the discovery was overrated and exaggerated and that, as a result of their statements, the stock would (go down) in price, and therefore I sold it." Mr. Stout testified that he had bought TGS stock for long-term appreciation; that he had no need for money when he sold it; and that the money received from the sale he put into a bank savings account. He stated: "I received that information. Whether I read it or heard it through the news media, I do not recall; but the essence of the information of the release is what I based the sale of my stock on."

One of the allegations in the Stout complaint is the following:

> "Confused by conflicting reports issued by defendants of the value of the Kidd 55 segment, plaintiffs sold their 1,000 shares on or about April 22, 1964, at a price of $42.00 per share."

The Stouts ask for rescission, or, in the alternative, damages, contending that the actions of defendants in preparing, issuing and causing the news release dated April 12, 1964, to be published were fraudulent; that the release misstated or concealed the true facts concerning the magnitude of the mineral discovery; that defendants knew the facts given were incorrect and misleading and knew, or should have known, that the facts as stated would be relied upon by shareholders. The court thinks these statements constitute a fair appraisal of the nature, purpose and effect of the April 12, 1964, news release.

Damages

It is unnecessary for the court to make any determination as to whether defendants were required by the statute or the rule to disclose the results of drilling at any time prior to April 12, 1964. Likewise, nothing would be gained by exploring the question whether the wide-spread rumors

in Canada and in this country gave rise to a duty on the part of the defendants to make a disclosure prior to that date.

The important fact is that defendants chose to issue a public statement, which both the statute and the rule required be accurate, fair and complete. Instead, the press release issued by defendants was misleading, intentionally deceptive, inaccurate and knowingly deficient in material facts pertaining to the results of drilling. The record establishes that each of the plaintiffs relied upon the misleading and inaccurate announcement in making his decision to sell his TGS stock. Consequently, defendant Texas Gulf Sulphur must respond in damages.

The aim of courts in cases of this type is to put the plaintiffs in the positions they would have been in if they had not been motivated by defendants' fraudulent press release to sell their stock. In this connection it is significant to point to the periods of time plaintiffs had held their stock. Plaintiff Reynolds, when he sold 500 shares of TGS stock on April 16, 1964, had held 300 shares since January 7, 1960, a period of more than four years, and had held 200 shares since May 18, 1962, a period of 23 months. Plaintiffs Stout sold 1000 shares of TGS stock on April 21, 1964. They had held those shares since February 5, 1962, more than two years. Plaintiff Mitchell purchased 420 shares of TGS stock at various times during the period December 11, 1953 and May 17, 1962. Some of the 400 shares he sold on April 17, 1964, he had held for more than 10 years, some about two years.

The variety of situations in which a 10(b) or 10b-5 violation may be found makes it difficult to formulate a comprehensive rule of damages. In the case of *J.I. Case Company* v. *Borak*, 377 U.S. 426, where violations of the Securities Exchange Act were involved, the Supreme Court observed that it is the duty of the courts to be alert to

provide such remedies as are necessary to make effective the congressional purpose, that where federally secured rights are invaded federal courts should adjust their remedies so as to grant necessary relief, and that they may use any available remedy to make good the wrong done.

Section 28(a) of the Securities Exchange Act[21] provides that "no person permitted to maintain a suit for damages under the provisions of this title shall recover * * * a total amount in excess of his actual damages * * *", but it provides no help in determining how "actual damages" are to be measured.

It seems to this court that the true and just measure of damages in these cases should be, with some qualification, what long ago came to be called the New York Rule. Of necessity, it was unthinkable that the common law rule in trover for the conversion of ordinary chattels, i.e., fair market value at time of conversion, should be applied in the case of corporate shares with rapidly changing values. So the rule evolved that the measure of damages in stock transactions is the highest intermediate value reached by the stock between the time of the wrongful act complained of and a reasonable time after the injured party received, or should have received notice of it, a time within which he has a reasonable opportunity to replace the stock. This was announced by the United States Supreme Court in a case decided in 1888 which arose in the Territory of Utah, *Galigher* v. *Jones*, 129 U.S. 194, 200-202.[22]

Factors considered in making the judgment on damages in this case include: the rapidity of price fluctuations in normal trading situations on the New York market, the excessive publicity, first having a tendency to depress the

21. 15 U.S.C. Sec. 78bb(a).

22. The former rule of highest intermediate value up to time of trial was repudiated.

price of Texas Gulf Sulphur shares, and later to cause it to rise, the nature of the Texas Gulf Sulphur enterprise, that is, a mining venture carrying on world wide mineral explorations, about which there has been extensive continuing publicity, all of which reasonably might have been expected to cause stockholders' interest to be stimulated and to cause them to be on the alert for sudden changes in the quotations, and to exercise ordinary care, prudence, and diligence in watching out for their own interest, and to learn of the Texas Gulf Sulphur announcement of April 16.

The obligation of the plaintiff shareholder is to exercise ordinary and reasonable care and diligence to look out for himself. The notice required is that which he received, or should have received, in the exercise of reasonable care and diligence.

We must draw the line somewhere, and this is an attempt to give a twenty trading day period within which the average of the highest daily prices is the measure of damages, and a period within which the shareholders received, or should have received, notice of the Texas Gulf Sulphur announcement of April 16.

A few days, is too short a time reasonably to expect stockholders to make a judgment and sell their stock, and much too early to let the New York market reflect the true value, over-stimulated upward or downward. The average of the highest daily sales for the 16th of April and 19 trading days subsequent thereto allows the market reactions more truly to reflect actual value and allows a more reasonable period of time within which to require the shareholders, in the exercise of ordinary diligence and prudence, to learn of the Texas Gulf Sulphur announcement of April 16 and to protect their interest.

There remain a couple of additional factors considered by the court in reaching the judgment in this case. They were suggested in Judge Henry J. Friendly's opinion in the

Second Circuit, *Securities and Exchange Commission* v. *Texas Gulf Sulphur*, 401 F.2d 864, 866-867.

Judge Friendly was speaking of "negligence" in the drafting of the release. Instead, the record here discloses that the press release issued by defendants was misleading, intentionally deceptive, inaccurate and knowingly deficient in material facts.

One of the choices open to the corporation, if it decides to speak, is to tell the truth.

The measure of damages here adopted is calculated to result in fair, reasonable and just awards. The damages awarded are compensatory and not punitive or *in terrorem*. Plaintiffs are only to be made whole, not to be compensated twice. When plaintiffs recover compensation for their losses from Texas Gulf Sulphur their claims against Fogarty will be deemed paid, satisfied and discharged.

On the day, April 16, 1964, that TGS publicly acknowledged that it had made a substantial mineral discovery, its stock advanced nearly $7 to a high of $37. The following day it advanced to a high of $42, and on the next trading day it advanced to a high of $44. This was followed by a decline to a high of $41¼, then an increase of more than 5 points to a high of $47. On April 29, 1964, it reached a high of $59. After a number of declines and a few advances it reached $60.50 on May 18, 1964. The extent to which the stock fluctuated on each trading day, and from day to day, is apparent from the table set out in the footnote.[23]

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23. The opening, high, low and closing prices of TGS stock for 20 trading days starting with April 16, 1964, are as follows:

		Open	*High*	*Low*	*Close*
April 16, 1964	(Thurs.)	30–⅛	37	30–⅛	36–⅜
April 17, 1964	(Fri.)	39–¾	42	38–¾	40–¼
April 20, 1964	(Mon.)	42	44	41–½	42–¼
April 21, 1964	(Tues.)	41	41–¼	39–⅛	40–⅛
April 22, 1964	(Wed.)	40–½	47	40–½	45–½

[*footnote continued on next page*]

In Section 151 of the Restatement of Restitution it is recognized that while generally the measure of recovery will be the value of the property at the time of its improper acquisition, retention or disposition, a "higher value" may be recognized "if this is required to avoid injustice where the property has fluctuated in value or additions have been made to it." Comment c. to Section 151 explains:

> "Where the subject matter is of fluctuating value, and where the persons deprived of it might have secured a higher amount for it had he not been so deprived, justice to him may require that the measure of recovery be more than the value at the time of deprivation. This is true where the recipient knowingly deprived the owner of his property or where a fiduciary in violation of his duty used the property of the beneficiary for his own benefit. In such cases the person deprived is entitled to be put in substantially the position in which he would have been had there not been the deprivation, and this may result in granting to him an amount equal to the highest value reached by the subject matter within a reasonable time after

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[*footnote continued from preceding page*]

		Open	*High*	*Low*	*Close*
April 23, 1964	(Thurs.)	47–3/4	48–1/4	42–1/8	42–5/8
April 24, 1964	(Fri.)	44	44–3/4	42–3/4	44–1/4
April 27, 1964	(Mon.)	44–7/8	47–1/2	44–5/8	47
April 28, 1964	(Tues.)	47–3/4	52–3/8	47–3/4	52–3/8
April 29, 1964	(Wed.)	54–1/2	59	53–1/2	56–3/4
April 30, 1964	(Thurs.)	54–1/2	58–3/8	54–1/2	54–3/4
May 1, 1964	(Fri.)	55–3/4	56–7/8	52–1/2	52–7/8
May 4, 1964	(Mon.)	54–1/2	54–5/8	52–1/8	52–5/8
May 5, 1964	(Tues.)	51–3/4	52	48–3/8	48–3/8
May 6, 1964	(Wed.)	48–1/4	52–1/4	46–3/8	52–1/4
May 7, 1964	(Thurs.)	52–1/2	53–3/8	49–1/2	49–1/2
May 8, 1964	(Fri.)	51–1/2	54–1/2	50–1/4	54–1/8
May 11, 1964	(Mon.)	54–7/8	57	54–5/8	56
May 12, 1964	(Tues.)	55–7/8	56–3/8	53–1/2	55
May 13, 1964	(Wed.)	54–1/4	55–7/8	51–5/8	51–5/8

the tortious conduct. This is done if he can prove that he probably would have made a sale while the subject matter was at its highest point in value * * *"

In the wrongful conversion case of *Nephi Processing Plant* v. *Talbot,* 247 F.2d 771 (10th Cir. 1957) the Circuit Court held that while Utah courts have recognized that as a general rule the measure of damage for conversion of property is the value of the property at the time of conversion "the rule has no application where the converted chattels are of a kind which have a fluctuating market value." In such cases, the court said, "the measure of damages is the highest market price of the property within a reasonable time after the owner has notice of the conversion."

What a "reasonable time" may be will vary from case to case. Here, a period of wide-spread rumors about a mineral discovery was followed by the deceptive and inaccurate press release published April 13, 1964, and the public announcement of a major discovery on April 16, 1964. On that day the price of TGS stock jumped about $7, and for the next 9 trading days the stock steadily increased, except for two days on each of which the closing price of the stock decreased about $2. On the 10th trading day (including the day of the announcement) the stock had advanced from approximately $30 to a high of $59. During the ensuing 11 days the stock fluctuated considerably and then climbed to a new high for this period of $60.50 on May 18, 1964.

In the circumstances of these cases the court considers that a reasonable period would be 20 trading days including April 16, 1964, the day of the announcement.

If the plaintiffs had not been led to sell their TGS shares and learned on April 16th, through the TGS announcement, of the proportions of the discovery, it would

be highly improbable, to say the least, that any one of them would have sold at the highest price.

The court deems it fair and just therefore, to take the average of all of the highest market prices on the 20 trading days, rather than the single highest market price during the period.

The average of the high market prices during such 20-day period is $50.75, which the court adopts as the measure of damages in these cases.

Damages to be awarded to plaintiff Reynolds are computed by deducting from $50.75 the price he received for each share, $33.625, and multiplying the resulting figure of $17,125 by 500, the number of shares he sold, to arrive at damages of $8,562.25. Interest on that amount at the rate of 6% per annum from the date he sold his stock to the date of judgment is allowed.

Similarly, damages for Plaintiff Mitchell are computed by deduction from $50.75 the amount received by him for each share and multiplying the resulting figure by the number of shares to arrive at damages of $4,390.00. In the case of Plaintiffs Stout, damages are awarded in the sum of $8,750.00, arrived at in the same manner. In each case interest is awarded at the rate of 6% per annum on the damages from the date on which the TGS shares of stock were sold to the date of judgment.

The court does not overlook the claims of the Stouts that (1) they did not learn of the "possibility" of an action against defendants until "on or after July 12, 1966" and (2) that they "did not become aware of or learn of the defendants' unlawful actions in connection with the issuance of the April 12, 1964, press release until on or about July 12, 1966." Aside from doubts the court has as to the credibility of these claims, he believes that in the circumstances of this case the Stouts knew, or should have known, of the misrepresentations and deceptions in the April 12, 1964, release within a period of 20 trading days.

STATUTE OF LIMITATIONS

There is no federal statute of limitations which is applicable to violations of Section 10(b) of the Act or of Rule 10b-5, consequently the Utah statute of limitations, 78-12-26(3) Utah Code Annotated, 1953, controls. It provides:

> "Within three years: * * *
>
> "(3) An action for relief on the ground of fraud or mistake; but the cause of action in such case shall not be deemed to have accrued until the discovery by the aggrieved party of the facts constituting the fraud or mistake * * *"

The action brought by Plaintiff Reynolds was filed July 12, 1966, and the action brought by Plaintiffs Stout was filed April 7, 1967. Each of these actions was clearly within the statutory period.

The action commenced by Plaintiff Mitchell was filed April 17, 1967. Defendants contend this action should be dismissed as having been filed too late. Mitchell, a C.P.A., testified at the trial that on April 16, 1964, the first free day after the close of the income tax season, he visited one of his brokers and for the first time learned of the press release of April 12, 1964. He went back to his office, obtained the certificate for 400 shares of TGS stock and took it to another broker and gave him an order to sell. At that time he realized he had an additional 20 shares and he told the broker he would bring them in the next day, which he did and gave the order to sell the 20 shares on April 17. He testified that at the time he gave the orders to sell he knew of no press release from TGS other than that of April 12, 1964. In a deposition taken by defendants, Mitchell testified in response to questions as follows:

> "Q. Do you recall any conversation with Mr. Lewis with respect to your Texas Gulf Sulphur stock after

the conversation on the 16th at approximately 1:00 o'clock or 1:30 that you have just described to us?

"A. You mean that same week?

"Q. Yes, any time.

"A. Yes, I believe it was Wednesday or Thursday of the following week that I think Mr. Singer told me —I am not too sure—or did I read it in the Wall Street Journal something to the effect that a new release had come out on the 16th."

The Court has examined and considered the testimony of Mr. Mitchell and the rather extensive depositions taken by defendants of Mitchell and his brokers, and has concluded that the above quoted testimony should be accepted. Consequently, Mitchell's action was filed within the time limit set by the Utah statute.

Dated this 9th day of January, 1970.

/s/ Willis W. Ritter
WILLIS W. RITTER, CHIEF JUDGE

Filed: January 13, 1970

Appendix A

Judgments of the District Court (Entered January 13, 1970)

UNITED STATES DISTRICT COURT

DISTRICT OF UTAH, CENTRAL DIVISION

C-62-67

WALTER A. MITCHELL,

Plaintiff,

v.

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

Defendants.

The above-captioned matter was consolidated for trial with three other cases, George Gordon Reynolds v. Texas Gulf Sulphur Company, et al. (Civil No. C-132-66), Arthur R. Stout, et al. v. Texas Gulf Sulphur Company, et al., and Lawrence L. Karlson et al. v. Texas Gulf Sulphur Company, et al. (Civil No. C-59-67), and the consolidated matter was tried to the Court, sitting without a jury, the Honorable Willis W. Ritter, Chief Judge, presiding, the plaintiff Walter A. Mitchell being represented by Roy G. Haslam, Esq., and the defendants Texas Gulf Sulphur Company and Charles F. Fogarty being represented by Calvin A. Behle, Esq., Keith E. Taylor, Esq., Orison S. Marden, Esq., and P. B. Konrad Knake, Esq., and the Court having received

certain stipulations of fact entered into by the parties and having received evidence, both testimonial and documentary, and having heard the arguments of counsel and being fully advised in the premises, and having filed its Amended Findings of Fact and Conclusion of Law:

IT IS HEREBY ORDERED, ADJUDGED AND DECREED:

That plaintiff be awarded judgment against defendants in the sum of $4,390.00, together with interest thereon at the rate of six per cent (6%) per annum to the date of judgment herein, and costs incurred in the maintenance of this action. Interest shall be calculated from April 16, 1964, to the date of judgment herein on that portion of the total damages incurred through the sale of 400 shares of Texas Gulf Sulphur Company stock, and from April 23, 1964 to the date of judgment herein on that portion of the total damages incurred through the sale of 20 shares of Texas Gulf Sulphur Company stock.

Dated this 13th day of January, 1970.

/s/ Willis W. Ritter
WILLIS W. RITTER, CHIEF JUDGE

Entered: January 13, 1970

C-132-66

GEORGE GORDON REYNOLDS,

Plaintiff,

v.

TEXAS GULF SULPHUR COMPANY, a Texas Corporation, and CHARLES F. FOGARTY,

Defendants.

The above captioned matter was consolidated for trial with the cases of Walter A. Mitchell v. Texas Gulf Sulphur Company, et al. (Civil No. C-62-67), Lawrence L. Karlson, et al. v. Texas Gulf Sulphur Company, et al. (Civil No. C-59-67), and Arthur R. Stout et al. v. Texas Gulf Sulphur Company et al. (Civil No. C-54-67), and the consolidated matter was tried to the Court, sitting without a jury, the Honorable Willis W. Ritter, Chief Judge, presiding, the plaintiff George Gordon Reynolds being represented by Parker M. Nielson, Esq., and A. Reed Reynolds, Esq., and the defendants Charles F. Fogarty and Texas Gulf Sulphur Company being represented by Calvin A. Behle, Esq., Keith E. Taylor, Esq., Orison S. Marden, Esq., and P. B. Konrad Knake, Esq., and the Court having received certain stipulations of fact entered into by the parties and having received evidence, both testimonial and documentary, and having heard the arguments of counsel and being fully advised in the premises and having made and filed its Amended Findings of Fact and Conclusions of Law herein:

NOW, THEREFORE, it is hereby ORDERED, ADJUDGED AND DECREED:

That Plaintiff George Gordon Reynolds is granted judgment against the defendants in the amount of $8,562.50, together with interest thereon at the rate of six per cent (6%) per annum from April 16, 1964, to the date of entry of judgment herein, and costs incurred in the maintenance of this action.

Dated this 13th day of January, 1970.

/s/ Willis W. Ritter
WILLIS W. RITTER, CHIEF JUDGE

Entered: January 13, 1970

Appendix A

Opinion of the Court of Appeals (Decided April 26, 1971)

UNITED STATES DISTRICT COURT

TENTH CIRCUIT

MARCH, 1971, TERM

Nos. 280-70
281-70

WALTER A. MITCHELL,
Appellee and Cross-Appellant,

v.

TEXAS GULF SULPHUR COMPANY, *et al.*,
Appellant and Cross-Appellee.

Nos. 282-70
283-70

GEORGE GORDON REYNOLDS,
Appellee and Cross-Appellant,

v.

TEXAS GULF SULPHUR COMPANY, *et al.*,
Appellant and Cross-Appellee.

Nos. 284-70
285-70

ARTHUR R. STOUT, *et al.*,
Appellees and Cross-Appellants,

v.

TEXAS GULF SULPHUR COMPANY, *et al.*,
Appellant and Cross-Appellee.

Appeal from the United States District Court for the District of Utah, Central Division

Appendix A—Opinion of the Court of Appeals

Before LEWIS, Chief Judge, HILL and McWILLIAMS, United States Circuit Judges.

HILL, Circuit Judge.

Appellees and cross-appellants Reynolds, Mitchell and Stout instituted actions in the Utah district against appellants and cross-appellees Texas Gulf Sulphur Company (hereinafter referred to as TGS) and Charles A. Fogarty, one of the principal officers of the company, to recover damages for violations of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b) and Rule 10b-5, 17 C.F.R. §240.10b-5, promulgated thereunder. The actions were consolidated for trial to the court without a jury and plaintiffs procured judgments in the three cases.[1]

While the complaints of the several parties make varying allegations of legal infractions,[2] the cases were tried, and are appealed, only upon alleged violations of Section 10(b) and Rule 10b-5, with a cross-appeal by Reynolds and Mitchell on the issues of damages and class action claims. Specifically, the claim is that appellees were damaged by the violations of TGS and Fogarty, its executive vice president, (1) for failure to disclose on April 12 and prior to April 16, 1964, information as to the results of drilling at the Timmins property; and (2) in issuing an inaccurate, misleading and deceptive press release published April 13, 1964.

The essential facts are as follows: Reynolds, Mitchell and Stout were and had been for several years stockholders in TGS. After several years of extensive mineral exploration on the Canadian Shield of eastern Canada, TGS de-

1. The trial court's opinion, including findings and conclusions, is reported in 309 F.Supp. 548.

2. One complaint included a count in common law fraud, another alleged a conspiracy to violate the Act and Rule, and one alleged violation of fiduciary duties and violations of Section 9 of the Act.

tected a promising anomoly on a plot of land known as the Kidd 55 segment near Timmins, Ontario, Canada. In November, 1963, TGS core-drilled the anomoly at its "strongest" point. The hole was designated K-55-1 and was completed November 12 at a depth of 655 feet. High ore content was indicated by visual examination, and after the core was split and sent to Utah for assay, it disclosed an average mineral content of 1.18% copper, 8.2% zinc, and 3.94 ounces of silver per ton, over a length of 602 feet. In response to the preliminary results, the TGS chief geologist wrote in a November 14, 1963, memorandum that this was "obviously of ore-grade"[3] but that "a great deal of caution must be exercised in extrapolating this intersection to tonnage estimates."

At this stage of the operations TGS owned only a fraction of the Kidd 55 property. Extreme precautions were taken to the end that no outsider would gain knowledge of the results of the explorations. By March, 1964, TGS had acquired without difficulty substantially all interest in the promising acreage adjacent to the drill site.

On April 7, 1964, K-55-3 was completed. The mineral content, by visual examination of the core, compared favorably with K-55-1 and eliminated the chances that the latter had been drilled "down dip". This hole aided in roughly establishing the east-west boundaries of the sulfite ore body. K-55-4 was completed to a 578 foot depth by 7:00 p.m., April 10, and produced a core comparable to K-55-1 and -3. K-55-4 had been drilled 200 feet south of K-55-1, on a 45 degree angle toward the west. Holes K-55-5 and K-55-6 had been started and were drilling by 7:00 p.m., April 10. K-55-5, 200 feet north of K-55-1 and on a 45 degree angle to the west, had encountered substantial copper mineralization over 42 feet of the 97 feet then drilled. K-

3. "Ore" is a word of art which indicates a body of commercially minable minerals.

55-6, 300 feet east of K-55-1 and on a 60 degree angle to the west, had encountered substantial copper mineralization over the last 127 feet of the 569 foot hole.

Between 7:00 p.m., April 10 and 7:00 p.m., April 12 (the evening prior to the first release) more data became available. K-55-5 was at the 531 foot level and had continued to encounter substantial copper mineralization over that entire length. During the same interval, K-55-6 had reached a depth of 881 feet and had found mineralization over the length of this intermediate drilling. Meanwhile, K-55-7 was started approximately 400 feet north of K-55-1 on a westerly 45 degree angle and was at 91 feet and showing mineralization. And K-55-8 was drilling at a depth of 162 feet without report as to its mineral content.

By the morning of April 13, K-55-5 had encountered substantial copper mineralization to the 580 foot mark; K-55-6 had found mineralization to the 946 foot level; and 50 feet of the 137 feet drilled at K-55-7 showed mineralization. By April 16, K-55-1, -2, -3, 4, -5, -6, and -8 were completed. K-55-7 was at 613 feet, -9 was at 373 feet, and -10 was at 123 feet. In a thumbnail sketch, this illustrates the rapid fire manner in which data was being accumulated at the Timmins drill site.

Although TGS sought to suppress the nature and extent of its discovery at Timmins, by early 1964, rumors had begun to generate excitement about the alleged strike. By April, 1964, property within several miles of the TGS site had been "staked". Canadian newspapers carried the rumors, and of their effect on the Toronto Stock Exchange, proclaimed by one to be "the wildest speculative spree since Nineteen Fifties." Eventually the rumors worked south to the United States.

On Saturday, April 11, 1964, both the New York Times and the Herald Tribune carried stories on the rumored

strike.[4] In response to the Times and Herald Tribune articles, the president of TGS directed Fogarty to prepare an official TGS statement. The president, a vice president and Fogarty all agreed that they could not responsibly conclude that a commercial ore body existed and that no calculations as to the size or grade of ore could be made without further drilling. Fogarty then drafted a statement based upon data gathered as of 7:00 p.m., April 10, and he released the statement Sunday afternoon, April 12.[5]

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4. The Herald Tribune article follows in part:

"The biggest ore strike since gold was discovered more than 60 years ago in Canada has stampeded speculators to the snowbound old mining city of Timmins, Ontario, some 450 miles northwest of Toronto.

"This time it's copper. Texas Gulf Sulphur Co., Ltd., which reportedly has made an unparalleled find in the Big Water Lake area about 15 miles north of Timmins, would not confirm reports of the strike.

"* * *.

"The story of the strike goes something like this: * * * The richness of the copper it [TGS] discovered was so great that samples reportedly were flown out of the country to be assayed.

"The huge lode is supposed to consist of a bed of coppe sulfite 600 feet wide with a possible overall copper return of 2.87 per cent through most of its width. * * *

"But the richest yield comes from the first 100 feet of that 600 foot belt. It is supposed to be 5.6 per cent, a bonanza if the story proves more than just a myth. But myth it may be.

"* * *.

"PCE Explorations reportedly is the company which worked with Texas Gulf Sulphur to make the strike.

"* * *.

"Sources in Timmins said four diamond drilling machines are working on Texas Gulf land, with four more machines slated to begin drilling next week. * * *"

5. "During the past few days, the exploration activities of Texas Gulf Sulphur in the area of Timmins, Ontario, have been widely reported in the press, coupled with rumors of a substantial copper dis-

[footnote continued on next page]

Appendix A—Opinion of the Court of Appeals

By TGS invitation, on April 13, a reporter from a Canadian mining journal, the Northern Miner, visited the Kidd-55 drilling site. The article detailing that visit was published April 16, and indicated that this "must be recorded as one of the most impressive drill holes completed in modern times." That same day, at 10:00 a.m. Eastern Standard Time, Fogarty held a second press conference and released a statement which revealed in some detail the

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[*footnote continued from preceding page*]

covery there. These reports exaggerate the scale of operations, and mention plans and statistics of size and grade of ore that are without factual basis and have evidently originated by speculation of people not connected with TGS.

"The facts are as follows. TGS has been exploring in the Timmins area for six years as part of its overall search in Canada and elsewhere for various minerals—lead, copper, zinc, etc. During the course of this work, in Timmins as well as in Eastern Canada, TGS has conducted exploration entirely on its own, without the participation by others.

"Numerous prospects have been investigated by geophysical means and a large number of selected ones have been core-drilled. These cores are sent to the United States for assay and detailed examination as a matter of routine and on advice of expert Canadian legal counsel. No inferences as to grade can be drawn from this procedure.

"Most of the areas drilled in Eastern Canada have revealed either barren pyrite or graphite without value; a few have resulted in discoveries of small or marginal sulphide ore bodies.

"Recent drilling on one property near Timmins has led to preliminary indications that more drilling would be required for proper evaluation of this prospect. The drilling done to date has not been conclusive, but the statements made by many outside quarters are unreliable and include information and figures that are not available to TGS.

"The work done to date has not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly misleading. When we have progressed to the point where reasonable and logical conclusions can be made, TGS will issue a definite statement to its stockholders and to the public in order to clarify the Timmins project. * * *"

magnitude of the discovery at Timmins.[6] Summaries of this announcement appeared on the private wire service of Merrill Lynch and on the Dow-Jones wire service shortly thereafter.

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6. "Texas Gulf Sulphur Company has made a major discovery of zinc, copper and silver in the Timmins area of Ontario, Canada.

"We announced last Sunday that when Texas Gulf had done sufficient work to reach firm conclusions, the company would issue a definite public statement on the Timmins project. We are now prepared to make that statement.

"Just ten days ago TGS had but one drilling rig operating in this area. As we state in our release of April 12, initial drilling on this one prospect had led to preliminary indications that more drilling would be required for proper evaluation. We immediately moved in additional drills so that by April 12 four drills were operating. With four drills, considerably more data has been accumulated.

"Seven drill holes are now essentially complete and indicate an ore body of at least 800 feet in length, 300 feet in width and having a verticle depth of more than 800 feet.

"We have not yet delimited the ore body in either direction along the strike. We have only drilled to a vertical depth of 800 feet. Values remain consistent to that depth.

"This is a major discovery. Preliminary data indicate a reserve of more than 25 million tons of ore. The only hole assayed so far represents over 600 feet of ore, indicating a true ore thickness of nearly 400 feet. The hole is described as follows:

> "Overburden is 24 feet. The initial core recovered showed 1 per cent copper over 24 feet. This was followed by a heavy chalcopyrite section of 82 feet, which assayed 7 per cent copper, 9.7 per [sic] zinc, and 2.4 ounces of silver. An additional 20 feet of massive sulphide assayed 12 per cent zinc. Disseminated sphalerite occurred through the following 44 feet of rock and this section assayed nearly 5 per cent zinc. A silver-rich zone of 36 feet followed, assaying 0.8 per cent copper, 13 per cent zinc, and 10.5 ounces of silver. An additional 16 feet assayed 4 per cent zinc and over 5 ounces of silver.
>
> "The following 100 feet was zinc-rich and assayed 0.33 per cent copper, 14.3 per cent zinc and 4 ounces of silver. A 106 foot section of core assaying 8 per cent zinc and 7.2 ounces of silver followed 36 feet of massive pyrite, assaying 3.4 per cent zinc, and 4 ounces of silver. A graphitic zone for the following 86

[*footnote continued on next page*]

Reynolds, Mitchell and the Stouts testified that they sold their TGS stock after hearing of the April 12 release but before becoming aware of the April 16 release. Sometime after the first release was published, Reynolds' broker in Salt Lake informed him as to its general content. On April 16, the broker relayed rumors that TGS had made a strike but in the broker's judgment this was mere propaganda. Reynolds then testified that he decided "to get out while the getting was good," whereupon he sold his 500 shares. Later that afternoon he learned of the favor-

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[*footnote continued from preceding page*]

feet contained approximately 4 per cent zinc and 2 ounces of silver. The final 20 feet assayed 8.3 per cent zinc and 2 ounces of silver. The overall interval of mineralization which could be mined in an open pit operation averaged 1.18 per cent copper, 8.1 per cent zinc, and 3.8 ounces of silver over a core length of 602 feet. The true width of the overall mineral zone is approximately 400 feet.

"Visual examination of cores from the other holes indicates comparable grade and continuity of ore.

"The ore body is at shallow depth, having only some 20 feet of overburden. This means that it can easily be mined initially by the open pit method.

"This discovery is in the northeast part of Kidd Township, and is about ten miles north of the Timmins airport.

"Our land position is favorable. Texas Gulf holds the mineral rights in 70 per cent of Kidd Township and has substantial acreage in the adjacent townships.

"TGS has been exploring in the Timmins area for some six years, using its own geophysical methods, followed by core drilling. Many prospects were drilled before this strike.

"TGS is actively continuing in the area, and in addition to this discovery is presently drilling on another prospect in the same township. We are continuing our exploration and are proud of our small but exceptionally competent exploration staff.

"We are continuing to drill this structure as systematically and rapidly as possible to determine its limits. We hope to have more information concerning this important discovery at the time of our stockholders' meetnig on April 23 in Houston, Texas."

able TGS report. He testified that had he known of the K-55-1 core results he would have doubled his holdings.

Mitchell visited his broker on the afternoon of the sixteenth, at which time he was referred to the April 12 release. He concluded that the stock would not sustain its current rise and gave instructions to sell 400 shares short against the box. Then, realizing he had failed to dispose of 20 shares, he delivered them on the seventeenth with similar sell instructions. According to his testimony, he had no knowledge of the April 16 release when he sold. After hearing about the April 12 release and that the TGS Timmins discovery was overrated, the Stouts gave orders to sell their 1,000 shares on April 21.

This controversy was tried to the court without a jury. On the basis of the testimony and exhibits produced at that trial, the district court made findings of fact and conclusions of law. To the extent that appellants' arguments rest upon a relitigation or reassessment of factual matters, we will defer to the trial court unless we are satisfied that they were clearly erroneous. Rule 52 F.R.Civ.P., 28 U.S.C. Fireman's Fund Ins. Co. v. S.E.K. Construction Co., Inc., —— F.2d — — (10th Cir. 1970); Butler Paper Co. v. Maneke-Kenzie Printing Co., 424 F.2d 247 (10th Cir. 1970); Knauff v. Utah Construction and Min. Co., 408 F.2d 958 (10th Cir. 1969).

The trial court found that the press release of April 12 was false, misleading, deceptive and fraudulent with respect to material matters disclosed by the company's drilling efforts; that the authors knew of the presence of ore-grade copper and zinc in major proportions; that the magnitude of the discovery was either misstated or concealed; and that TGS and Fogarty knew the press release statements were incorrect and misleading, and knew or should have known that the statements would be relied upon by shareholders. After finding that each appellee had relied on the April 12 release in selling his TGS stock, the court

awarded damages based on the average of the highest daily per share selling price between April 16, 1964, and May 13, 1964, twenty trading days following the last press release.

Rule 10b-5 is plain, concise and unambiguous. It provides as follows:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (1) To employ any device, scheme, or artifice to defraud,
>
> (2) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,
>
> in connection with the purchase or sale of any security.

Neither Rule 10b-5 nor Section 10(b) in terms grants a private right of action for the nonfeasance or malfeasances denoted in their language. But this is of miniscule significance in this litigation, presumably because such right has now been recognized in all the federal circuits which have had occasion to consider the issue.[7]

7. Bank of America National Trust and Savings Association v. Douglas, 105 F.2d 100 (D.C.Cir. 1939); Rogen v. Ilikon Corp., 361 F.2d 260 (1st Cir. 1966); Securities and Exchange Commission v. Texas Gulf Sulphur Co., 401 F.2d 833 (2nd Cir. 1968); McClure v. Borne Chemical Co., 292 F.2d 824 (3rd Cir. 1961); Rekant v.

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From its origin, the private right of recovery has been based on the general principle of tort law that violation of a provision of a criminal statute designed to prevent a particular type of harm can give rise to a civil remedy. Kardon v. National Gypsum Co., 69 F.Supp. 512 (E.D.Pa. 1946). In civil actions instituted on the basis of 10b-5 violations, the keynote of which is fraud, the full panoply of common law fraud elements—misrepresentation or nondisclosure, materiality, scienter, intent to defraud, reliance and causation—have crept in and played varying roles of significance. However, a number of these elements have diminished in importance in private actions, and we have stated in Stevens v. Vowell, 343 F.2d 374, 379 (10th Cir. 1965), that "[i]t is not necessary to allege or prove common law fraud to make out a case under the statute and rule. It is only necessary to prove one of the prohibited actions such as the material misstatement of fact or the omission to state a material fact." Notwithstanding, appellants urge that appellees have failed to establish the presence of most of the common law fraud ingredients, i.e., misrepresentation or nondisclosure of material facts, scienter, intent to defraud, reliance, and some semblance of privity. A full measure of our attention will be devoted to each of these constituent parts.

The misleading, misrepresented or untruthful character of the release may appear from the nature of the statement considered alone, or, when the facts are fully disclosed,

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[*footnote continued from preceding page*]

Desser, 425 F.2d 872 (5th Cir. 1970); Texas Continental Life Ins. Co. v. Dunne, 307 F.2d 242 (6th Cir. 1962); Jordan Building Corp. v. Doyle, O'Connor & Co., 401 F.2d 47 (7th Cir. 1968); City National Bank of Forth Smith, Ark. v. Vanderboom, 422 F.2d 221 (8th Cir. 1970); Ellis v. Carter, 291 F.2d 270 (9th Cir. 1961); Gilbert v. Nixon, 429 F.2d 348 (10th Cir. 1970); and impliedly in J.I. Case Co. v. Borak, 377 U.S. 426, 84 S. Ct. 1555, 12 L.Ed.2d 423 (1964) and Surowitz v. Hilton Hotels Corp., 383 U.S. 363 (1966).

from the half truths, omissions or absence of full candor concealed therein. *See* Gilbert v. Nixon, 429 F.2d 348, 356 (10th Cir. 1970); Meisel v. North Jersey Trust Company, 218 F.Supp. 274 (S.D.N.Y. 1963); Cochran v. Channing Corporation, 211 F.Supp. 239 (S.D.N.Y. 1962). Misrepresented or omitted facts become material, hence actionable under 10b-5, when, considering the complaining parties as reasonable investors, the disclosure of the undisclosed facts or candid revelation of misleading facts would affect their trading judgment. *See* Gilbert v. Nixon, supra; S.E.C. v. Texas Gulf Sulphur Company, 401 F.2d 833, 849 (2nd Cir. 1968), *cert. den'd sub nom.* Coates & Kline v. S.E.C., 394 U.S. 976 (1969); Rogen v. Ilikon Corporation, 361 F.2d 260, 266 (1st Cir. 1966); List v. Fashion Park, Inc., 340 F.2d 457, 462 (2nd Cir. 1965), *cert. den'd sub nom.* List v. Lerner, 382 U.S. 811 (1965). The implicit variables to be weighed in a materiality analysis are the magnitude and probability of the occurrence of the event, set against the size and total activity of the subject company.

The trial court found the April 12 release "inaccurate, misleading and deceptive with respect to material matters." Reynolds v. Texas Gulf Sulphur Co., 309 F.Supp. 548, 559 (D.Utah 1970). We agree upon the following recitation of facts found in the record.

To put the chronicle of events in perspective, it must be remembered that from the drilling of K-55-1 in late 1963, no serious drilling activity had transpired until March 31, 1964. On the basis of the core analysis then available to them, the corporate leaders committed themselves to secrecy regarding the "prospect" until the adjacent property could be acquired. Once substantial holdings in contiguous realty was accomplished, drilling activity again came to life with renewed vigor. As of April 10, three drilling rigs were operating, with another to begin drilling on April 12, in an obvious effort to ascertain the dimensions of the min-

eral body. Daily reports on drilling progress continuously altered the measurements of the body, but the mineralization content continued to retain the same characteristics as the core from K-55-1. The data available to TGS at the time of the first press release was ample to have accorded with a more complete, thereby favorable, statement. The representation that "preliminary indications [are] that more drilling would be required for proper evaluation of this prospect" was not a statement candidly disclosing the available knowledge of TGS. Although the full magnitude of the ore body could not be precisely determined, the available information allowed more than a marginal possibility that a commercial "mine" existed.

The contested press release was issued during the afternoon of Sunday, April 12, and purported to be based on "work done to date" and "drilling done to date." This misrepresents and distorts the actual fact that the information upon which TGS formulated the release was current as of 7:00 p.m., April 10. Only in light of the rapid progression of available drilling information does this become forcefully significant. Between 7:00 p.m. on Friday and late afternoon the following Sunday, these developments occurred: (1) K-55-5 had been drilled another 471 feet to a depth of 531 feet; (2) K-55-6 had been drilled another 301 feet to a depth of 881 feet; (3) K-55-7 had been commenced and was at the 91 foot level; and (4) K-55-8 had been commenced and was at the 105 foot level. Thus at the time of the release, TGS drilling had established the rough east-west boundaries of the ore body (through K-55-1 and K-55-3) at nearly 300 feet; the zone of ore proceeded south at least 200 feet (K-55-4), strong mineralization was evident 200 feet north (K-55-5) with fair mineralization showing 400 feet north; and the depth was being ascertained (K-55-6) by an 881 foot hole which was still encountering mineralization at that level.

The recitation that "work to date has not been sufficient to reach definite conclusions and any statement as to size and grade of ore would be premature and possibly misleading" is a one-sided statement. No one could dispute that TGS could not have accurately defined the outer limits of the ore body as of April 12, but that is not the test. When TGS undertook to deny and clarify rumor and fact, they were bound to accurately depict the situation as they then knew it. The full magnitude may yet have been a mystery, but armed with the data available on the 12th, TGS was in a position to unveil the then known dimensions and drilling data of their discovery. Having failed to accurately portray what they knew, and commenting that the information was current when in fact it was sorely outdated, TGS misrepresented the facts of the Kidd 55 discovery.

To buttress the findings above, the trial court reiterated that the Northern Miner journalist who was permitted to visit Kidd 55 on April 13 was able to print a detailed story with the approval of TGS.[8] The agreement was that Ackerly would visit the drill site and on the basis of his observation, prepare an article for publication. But it was to be printed only after Mollison, a vice president in charge of the Timmins project, read, edited, and authorized its

8. Texas Gulf Sulphur has chalked up a brilliant exploration success * * * a major new zinc-copper-silver mine is definitely in the making. * * *

* * * On the basis of seven tests either completed or drilling, it can be stated that a strike length of 600 ft. minimum has been established showing an ore width of roughly 300 ft. which has been traced so far to a maximum vertical depth of about 800 ft. * * * This must be recorded as one of the most impressive drill holes completed in modern times.

From the dimensions already known, the Northern Miner can say that something in excess of 10,000,000 tons of ore is indicated. It is capped with something like 20 feet of overburden, presenting no stripping problems, and the steep dip and wide widths will lend themselves ideally to an open-pit mining situation.

printing. Just as the trial court, we believe this confirms the finding that TGS knew a great deal more than it told on April 12 and that by concealing, omitting or misrepresenting these facts they violated Rule 10b-5.

Even if it is for the moment assumed that some notation had been made that the information was not current, the release still was false, misleading and deceptive. The rumors were of a "substantial copper discovery." In effect, TGS answered without qualification that these rumors were "without factual basis." Then they proceeded to speak of most areas drilled as revealing "either barren pyrite or graphite without value; a few have resulted in discoveries of small or marginal sulphide ore bodies." It was then stated that more drilling would be required for proper evaluation. Not a single note of encouragement is contained in the entire April 12 release regarding the Kidd 55 drilling. The trial court found the release painted a bleak and gloomy picture, and we agree. The substance of the release was a complete denial of the rumors, without any attempt to relate the favorable prospects as shown by the core assay of K-55-1 and the visual examinations of cores from K-55-3, -4, -5 and -6. Each core, in its own way, added to the confirmation of an exceptional ore discovery. We do not now decide whether TGS would have had to make a statement on the 12th, absent the rumors. But with the described data available it was deceitful and fraudulent to speak as TGS did.

By the testimony of appellees' expert, on April 12, TGS knew or could have conservatively computed the reserves of Kidd 55 at 7,390,000 tons of ore valued at $183,740,000. And by the evening of April 12, sufficient data was available for TGS to calculate the reserves at 11,790,000 tons valued around $219,740,000. When the trial court, crediting this testimony over that tendered by appellants' expert, put those figures alongside the computation made in

the Northern Miner based on April 13 data indicating in excess of 10,000,000 tons, its finding as to inaccuracy and deception are well substantiated and thus sustained.

Appellants seek to diminish the credibility of appellees' expert, Dr. Christiansen, by pointing to his method of evaluating the reserves, by urging that his conclusions were based on post-April 10 drilling information and took into account the April 16 release, and it is charged that contemporaneous remarks made by the judge during trial served to discredit Dr. Christiansen's calculations. Addressing the last allegation first, the trial judge ultimately viewed Dr. Christiansen's testimony as credible and notwithstanding the contrary trial colloquy, we are bound by that unless there was clear error. Second, the method employed by appellees' expert did not deviate from professional norms and the proof of that is unerringly highlighted by the content of the April 16 release. Simply because one expert is willing to compute ore reserves upon given data where another refuses, does not destroy the credibility of the first nor improve the reliability of the latter. Dr. Christiansen carefully progressed through the daily series of test cores, logs, etc., and upon the then available data, computed the reserves on the basis of each day's drilling. We can find no error in trusting these computations.

These facts also provide ample foundation for the trial court's finding of materiality. K-55-1 had been assayed and was known to contain minerals of extraordinary quality. The cores from K-55-3 and K-55-4 were visually appraised to be of the same high quality, and the preliminary results of K-55-5, -6 and -7 expanded the limits of the ore body to commercially minable proportions. Additionally, the ore was near the surface to facilitate more economical strip mining. Even considering the size of TGS and its level of operations in international mineral exploration and development, the known size and quality of the ore

body was material information; that is, the trading judgment of reasonable investors would not have been left untouched upon receipt of such information. The trial court was unerringly correct.

TGS seeks refuge in the language of the New York Stock Exchange Company Manual which provides that in the face of rumors without factual basis or rumors which need clarification or interpretation, a quick and speedy denial is the recommended procedure.[9]

It would be an unwarranted contortion of this rule to enfold TGS within its protection. First, because of the facts heretofore set forth, it cannot be said that the rumors had no basis in fact. Second, an S.E.C. statement, relied upon by TGS to support their proposition, is contrary to the facts of this case. Directing its attention to rumors circulating about the Alaskan North Slope oil drilling activities, the Commission has warned investors against those rumors because of the intricacies and uncertainties of oil production on the North Slope. The S.E.C. has cautioned the oil companies "to weigh carefully the conclusions and interpretations of information they may use in statements released to the public." TGS has seized onto this language as a characterization of the action they took. But the S.E.C. continued: "While the absence of proved reserves does not preclude *factual disclosures* of exploratory activities, *such as information relating to drilling operations,* any statements which are made should be appropriately qualified to indicate the limitations upon the significance of the facts disclosed." [Emphasis added.]

9. "Occasions may arise when rumors have been circulated which have no basis in fact or which require clarification or interpretation and also which result in unusual activity or price changes in a particular security. Under such circumstances, the most effective procedure is the quick and speedy denial of such rumors through a release to the public press." [A-22]

The duty evolving upon a company facing these circumstances is to speak truthfully, accurately and with total candor as to the material facts. That is not too much to ask of any company with the interest of its shareholders central to its commentary. It is what the S.E.C. demands, what the law requires, and what every stockholder is entitled to. Sunray DX Oil Company v. Helmerich & Payne, Inc., 398 F.2d 447 (10th Cir. 1968), does not forbid this reasoning. In the context of the facts there present, the court felt that a detailed statement would not add to the informed status of investors, but would mislead them due to the nuances of technical terms used in divulging further information. The problems extant in that off-shore drilling case are not present in the instant controversy.

It is said that if the courts require factual data in statements such as that originally framed by TGS, issuance of statements will fall out of favor and use. The conjecture is that by requiring a complete statement of material facts, corporations will cease to issue them and the Act will be frustrated in its attempt to keep stockholders informed of material facts. We view this speculation untenable, for the duty to disclose facts when they become material has not been altered by this decision. Simply stated, when the material information is available and ripe for publication, the difficulties inherent in formulating a release cannot overbear the accuracy of the statements contained therein. Nor is it reasonable to conclude that the detail of a full release will preclude its publication in these circumstances. Indeed, the thoroughness of the April 16 release stands as evidence to the contrary.

Another argument of appellants is that as a predicate to a 10b-5 action, the corporation, its directors or other "insiders" must be trading in the market.[10] At minimum,

10. Although considerable trading had been done in the market by corporate "insiders" and "tippees", it was stipulated at trial that there was no illegal trading by the instant parties at or after the time of the April 12 release.

it is urged that a market purpose to benefit the alleged wrongdoer must be proven before recovery can be permitted. The attempt is to circumvent the language in SEC v. Texas Gulf Sulphur Company, 402 F.2d at 862: "Rule 10b-5 is violated whenever assertions are made * * * in a manner reasonably calculated to influence the investing public, e.g., by means of the financial media * * * if such assertions are false or misleading or are so incomplete as to mislead irrespective of whether the issuance of the release was motivated by corporate officials for ulterior purposes. It seems clear, however, that if corporate management demonstrates that it was diligent in ascertaining that the information it published was the whole truth and that such diligently obtained information was disseminated in good faith, Rule 10b-5 would not have been violated."

In its origin, 10b-5 was intended only to give sellers the same protection extended to buyers by other provisions of the Act, and did not contemplate protection of stockholders against a breach of fiduciary duty by corporate insiders. Within a few years, however, the federal courts ceased to look upon the Rule in the narrow context of seller protection and began to see in it a greater purpose, i.e., equalization of bargaining position of the parties on both sides of a transaction. A. Bromberg, Securities Law: Fraud—S.E.C. Rule 10b-5, §3.2 (200), (300), pp. 65-66 (1969) [hereinafter Bromberg]. But even with this expanded vision, the courts generally required, at minimum, "[a] semblance of privity between the vendor and purchaser of the security in connection with which the improper act, practice or course of business was invoked. * * *" Joseph v. Farnsworth Radio & Television Corp., 99 F.Supp. 701, 706 (S.D.N.Y. 1951).

The Second Circuit in the Texas Gulf Sulphur case expanded this rationale to include protection for open market investors, including speculators, when misled by nontrad-

ing insiders. After reviewing Congressional history, the court said: "Congress when it used the phrase 'in connection with the purchase or sale of any security' intended only that the device employed, whatever it might be, be of a sort that would cause reasonable investors to rely thereon, and, in connection therewith, so relying, cause them to purchase or sell a corporation's securities. * * * We do not believe that Congress intended that the proscriptions of the Act would not be violated unless the makers of a misleading statement also participated in pertinent securities transactions in connection therewith, or unless it could be shown that the issuance of the statement was motivated by a plan to benefit the corporation or themselves at the expense of a duped investing public." S.E.C. v. Texas Gulf Sulphur Company, 401 F.2d at 860. TGS invites this circuit to either part company with the Second Circuit rationale or distinguish it on the basis that it must be confined to S.E.C. enforcement actions.

The Second Circuit has laid to rest the argument that the new "connection" requirement be narrowly applied to S.E.C. enforcement actions. Following the TGS suit was Hiet v. Wietzen, 402 F.2d 909 (2nd Cir. 1968), a private action, wherein the TGS "connection" rule was applied. We also decline the invitation to ignore the forward looking view of the Second Circuit regarding the "connection" requirement. Perhaps the first step is to realize that the common law requirement of privity has all but vanished from 10b-5 proceedings[11] while the distinguishable "con-

11. Hiet v. Wietzen, 402 F.2d 909 (2nd Cir. 1968); Texas Continental Life Ins. Co. v. Dunne, 307 F.2d 242 (6th Cir. 1962); Rippey v. Denver U. S. National Bank, 260 F.Supp. 704 (D.Col. 1966); Miller v. Bargain City, U.S.A., Inc., 229 F.Supp. 33 (E.D.Pa. 1964); Freed v. Szabo Food Service, Inc. (N.D.Ill., filed Jan. 14, 1964); Bromberg, §8.5 (511) at 207; III Loss, Securities Regulations, Chap. 11C(c) at 1767-71 and VI Loss, Chap. 11C at 3890-97.

nection element is retained.[12] In its development, the cases have deemed the "connection" requirement fulfilled if the company has uttered false or misleading statements concerning the securities in question, provided the complainants have relied on the misrepresented facts. The result which we here support is that insider trading is not a requisite for 10b-5 violation by misrepresentation. As appropriately stated by the Second Circuit, "a corporation's misleading material statement may injure an investor irrespective of whether the corporation itself, or those individuals managing it, are contemporaneously buying or selling the stock of the corporation." S.E.C. v. Texas Gulf Sulphur Company, 401 F.2d at 861. The trial court had little difficulty finding from the testimony of Fogarty and other corporate officers that the April 12 statement was made in a manner reasonably calculated to influence the investing public. We concur.

But even if the release was made in connection with the sale of these securities, appellants further urge that the overwhelming weight of authority holds that scienter in some form is required in a private 10b-5 damage action. *See* VI Loss, Ch. 11C at 3883-90. In the Second Circuit, at least, that description appears to be correct. But while some degree of scienter is required, it does not equate with the intent to defraud required in a common law fraud action. Globus v. Law Research Service, Inc., 418 F.2d 1276 (2nd Cir. 1969); Hiet v. Wietzen, supra; Astor v. Texas Gulf Sulphur Company, 306 F.Supp. 1333 (S.D.N.Y. 1969). Contrariwise, in the Eighth Circuit, City National Bank of Fort Smith, Ark. v. Vanderboom, 422 F.2d 221 (8th Cir. 1970), and the Ninth Circuit, Ellis v. Carter, 291 F.2d 270 (9th Cir. 1961), the rule is that scienter is not required to maintain a private 10b-5 damage action. We have dealt

12. *See* Rippey v. Denver U.S. National Bank, supra; Stockwell v. Reynolds & Co., 252 F.Supp. 215 (S.D.N.Y. 1965); Milier v. Bargain City, U.S.A., Inc., supra.

with the issue under significantly different circumstances in Stevens v. Vowell, 343 F.2d 374 (10th Cir. 1965). But in Gilbert v. Nixon, 429 F.2d 348, 357 (10th Cir. 1970), we considered the identical issue in a case involving Section 12(2) and Rule 10b-5. The rule there articulated is applicable here. "One is not to be held liable * * * because of his misleading misrepresentation or omission of material fact, the truth of the matter being unknown to the purchaser, if the party responsible for the misrepresentation or omission sustains the burden of proving that he did not know, and in the exercise of reasonable care could not have known that it was a misrepresentation or omission."

Two times during his opinion the trial judge recited: "[T]he record here discloses that the press release issued by defendants was misleading, intentionally deceptive, inaccurate and knowingly deficient in material facts." Reynolds v. Texas Gulf Sulphur Company, 309 F.Supp. at 562, 563-64. Confronted with the abundance of evidence in the record, we cannot conclude that TGS sustained its burden of proving that it did not know of the misrepresentation, nor was it demonstrated that with due diligence TGS could not have known of the faultiness of the statement.

The complainants have met the reliance requirement if "the misrepresentation is a substantial factor in determining the course of conduct which results in [the investors'] loss." List v. Fashion Park, Inc., 340 F.2d 457, 462 (2nd Cir. 1965); VI Loss, Ch. 11C at 3876-83. Appellants' argument on this point is two-fold: First, that the trial court's findings that each plaintiff-appellee relied on the April 12 release was clearly erroneous; and, second, that as a matter of law, once the April 16 release was received by the brokerage houses over the Merrill Lynch and Dow-Jones wire services, curative information was available which should have corrected any erroneous notions in the minds of reasonable investors as to the Timmins project.

The trial court specifically found that each of the appellees herein relied upon the misleading and inaccurate announcement in making his decision to sell his TGS stock, and that none knew of the announcement of April 16 at the time of his sale. Reynolds v. Texas Gulf Sulphur Company, 309 F. Supp. at 559, 560, 561, 562. Appellants enumerate several factors which may have induced Reynolds to sell his TGS stock. A thorough search of the record convinces us that although any one or all of the factors may have partially motivated the sale, the evidence is not so deficient as to make the finding of the trial court clearly erroneous that the principal reliance was on the April 12 statement.

The dispute over the Mitchell sale is that he timed his decision to sell on speculation as to what the market was going to do. Again, the evidence of record does not clearly refute the finding that the primary motivation was the deceptive April 12 release. The Stouts' case is more difficult due to the time lapse between the corrective April 16 release and the sell order—more than five days later. But even with that entanglement, we cannot, on the basis of clear error, conclude from the record that the April 12 release was not a substantial factor in the Stouts' decision to sell.

Greater difficulty is encountered with the second of appellants' two-pronged argument which directs itself to the issue of due diligence and good faith required of investors trading in the market. *See* City National Bank of Fort Smith, Ark. v. Vanderboom, supra. Reynolds traded within a reasonably brief time following the April 16 release and should not be denied his recovery. Mitchell is in exactly the same position with regard to the 400 shares which were sold by April 17. Both testified that they were attempting to reap the maximum profit before the "gloomy" release took its toll. We conclude that good faith and due dili-

gence were exercised in the sale of these shares. On the other hand, although mala fides is not involved, the record will not support a claim of due diligence in the Stouts' sale and in Mitchell's late sale of the 20 shares.

At some point in time after the publication of a curative statement such as that of April 16, stockholders should no longer be able to claim reliance on the deceptive release, sell, and then sue for damages when the stock value continues to rise. This is but a requirement that stockholders too act in good faith and with due diligence in purchasing and selling stock. Although Mitchell alleges that he ordered the 20 shares sold on the 17th, there is no dispute that they were not in fact sold until the 23rd. His explanation is that somehow the sell order was not properly communicated until the 22nd, when he called his broker to inquire into their status. In the Stouts' case, there was no miscommunication. They simply did not intend to sell until the 21st. While in some circumstances such delays may not be unreasonable, we conclude that under the circumstances of this case it would unjustifiably extend TGS liability to intolerable limits.

Between April 13 and April 22, TGS stock had increased in value from 30⅛ to a high of 47, with the volume of sales going from 126,500 to over 326,000. But most significant is the abundance of publicity given the April 16 statement during the following few days. The business news of every major news publication carried the story with bold headlines. Indeed, the 45 pages of press clippings and stock quotations in the record gives force to the proportion that the April 16 release received saturation coverage. We conclude that by Wednesday, April 22 when the Stouts sold their stock, and Thursday, April 23 when Mitchell sold the 20 shares, the reasonable investor would have become informed of the April 16 release and could no longer rely on the earlier release in selling TGS stock.

The final defense asserted by appellants is directed to the applicable statute of limitations. There is no statute of limitations contained in Section 10(b) of the Act. The settled rule is that when a federal statute is silent as to the statute of limitations, the appropriate period of limitation of the forum state is applied. United Automobile Workers v. Hoosier Cardinal Corporation, 383 U.S. 696 (1966). The trial court in this case looked to Utah law and applied 78-12-26(3), Utah Code Annotated, 1953: "Within three years: * * * (3) An action for relief on the ground of fraud or mistake; but the cause of action in such case shall not be deemed to have accrued until the discovery by the aggrieved party of the fact constituting fraud or mistake."

Appellants contest the applicability of this fraud statute of limitations upon the tenet that this is not a fraud case. It is apparent, we trust, from the earlier statements in this opinion supporting the findings of the trial court, that the central issues in private 10b-5 damage actions coalesce with "fraud or mistake". Moreover, in Chiodo v. General Waterworks Corporation, 380 F.2d 860 (10th Cir. 1967), it was held that the Utah statute of limitations pertaining to fraud controlled the filing of a complaint under Section 10(b) of the Act. Vanderboom v. Sexton, 422 F.2d 1233 (8th Cir. 1970), is principally distinguishable because that circuit has abrogated any semblance of scienter in a private 10-b-5 damage action. Not having accomplished that same rationale in this circuit, we will here adhere to earlier decisions applying fraud statutes of limitations.

Some doubt still remains, however, whether appellees met this period of limitations. Reynolds filed suit July 12, 1966. No complaint is raised as to the appropriateness of his action meeting the three-year limit. But Mitchell did not file until April 17, 1967, and appellants claim that since he knew of the April 16 release on the date of its issuance, he knew of the fraud on that same day and is thus

not within the time limit for filing suit. Mitchell contended he did not know of the fraud until later. The matter rests on facts which the trial court found favorable to Mitchell, and we sustain that finding on an absence of clear error.

We pass now to the issue of damages. The trial court, in framing a rule for determining a proper award of damages, started with the proposition that the aim of courts in this situation is to restore claiming parties to the positions they would have enjoyed had they not been fraudulently induced to sell their stock. Proceeding to fashion a remedy which would make effective the Congressional purpose, J. I. Case Co. v. Borak, 377 U.S. 426, 433 (1964), the trial court adopted a qualification of the rule announced in Galigher v. Jones, 129 U.S. 193, 201 (1889): "[T]he true and just measure of damages in these cases is to be the intermediate value of the stock between the time of its conversion and a reasonable time after the owner has received notice of it to enable him to replace the stock." From this rule the trial court postulated the following measure of damages: "* * * this is an attempt to give a twenty trading day period within which the average of the highest daily prices is the measure of damages, and a period within which the shareholders received, or should have received, notice of the Texas Gulf Sulphur announcement of April 16." Reynolds v. Texas Gulf Sulphur Company, 309 F.Supp. at 563. With the lapse of twenty trading days it was felt that market reactions would more accurately reflect actual value and allow a reasonable time for the reasonable and diligent shareholder to learn of the April 16 announcement and protect his interest. The averaging aspect was inserted because the trial court felt it highly improbable that any of the appellees would have sold at the highest price.

All party litigants are dissatisfied with this measure of damages. Appellants contend that only actual damages based on market value as of April 16 are recoverable; that

appellees have failed to prove such loss; and even accepting the lower court's measure, twenty days is too lengthy and thereby unreasonable. By cross-appeal, Mitchell and Reynolds request restitution or damages equivalent to restitution, and costs of conducting this action.

We are in harmony with the rudiments of the trial court's measure of damages and alter that rule only to more closely adhere to the notion that the injured parties should be restored to their former status. The divergent approaches taken by the litigants verify the suspicion that a set rule of damages has not been tested in this kind of case. Furthermore, because of the uniqueness of the litigation, it would be unwise to set forth a uniform rule with broad applications to all securities cases. Thus, the rule styled by this court is fashioned for these unprecedented circumstances.

Restitution and damages equivalent to restitution are inappropriate remedies in this action. Traditionally these theories have been concerned with direct-personal dealings in which there is privity and/or unjust enrichment upon which to justify the remedy. Speed v. Transamerica Corporation, 135 F.Supp. 176 (D. Del. 1955), *aff'd modifying interest* 235 F.2d 369 (3rd Cir. 1956); Janigan v. Taylor, 344 F.2d 781 (1st Cir. 1965); Bromberg, § 8.1 at 225, et seq. Here neither element is present inasmuch as neither TGS nor Fogarty purchased appellees' shares of stock. The absence of those fundamental facts, plus the hardship it would visit upon TGS as a corporation,[13] makes this case inap-

13. In their appellate brief, appellants claim that if the measure of damages theory applied in the trial court is upheld on appeal, damages will approach $14,000,000. In Ruder, Texas Gulf Sulphur —The Second Round, 63 Nw. U. L. Rev. 423, 428-29 (1969), restitution damages are computed: "* * * if liability is imposed upon TGS in the private suits for the company's failure to disclose the material inside information which it possessed, its damages may be equal to $130 for every share traded during the period from No-

[*footnote continued on next page*]

propriate for any form of restitution, and the trial court properly rejected it.

We believe the measure of damages used should award the reasonable investor the amount it would have taken him to invest in the TGS market within a reasonable period of time after he became informed of the April 16 release. Through the testimony of both Reynolds and Mitchell we are satisfied, as was the trial court, that they possessed ample sophistication to fall within the nebulous reasonable investor category. By Monday, April 20, the diligent and reasonable investor was informed of the most recent TGS statement and as we earlier stated, after that duration a reasonable investor would not have relied upon the April 12 statement in selling his TGS stock. After the reasonable stockholder had opportunity to apprise himself of the April 16 release and its import to investment, a reasonable time lapse may be allowed to expire to permit the investor to decide whether or not he would reinvest and take advantage of a spiraling market. If he has failed to reinvest, as both Reynolds and Mitchell did, he must suffer the consequences of his own judgment. The award proposed would permit one to "cover" by reinvestment and suffer neither loss nor forced sale.

The damages then should be based on the highest value of TGS stock between Monday, April 20 and a reasonable time thereafter. Whether we conclude such duration should be an added nine trading days (through Friday, May 1)

[*footnote continued from preceding page*]

vember 12, 1963, through April 16, 1964. Since approximately 3 million TGS shares were traded during this period, damages would amount to over 390 million dollars, approximately 150 million dollars more than the present net worth of the company. If liability is imposed upon TGS only for the period from April 12, 1964, * * * until April 16, 1964, * * * the company could incur damages of about 84 million dollars, since approximately 691,000 shares were traded during that four day period." [Footnotes omitted]

which seems more reasonable in these circumstances, or the seventeen additional trading days imposed by the trial court (through Wednesday, May 13) is irrelevant to the award. For in either event, the highest value was achieved on Wednesday, April 29 (at $59) prior to the expiration of either time limit.

The averaging aspect is deleted to conform with what is considered the focal purpose: to award the reasonable investor an amount which offsets any loss he suffered by a deceitfully induced sale. To award an average price would not fully compensate him for a number of the days within the reasonable period following the last release. While this is an admitted compromise between the restitution rule and the actual damage approach as taken by TGS, it seems a fair way to reinstate stockholders who were wrongfully deprived of their gain because of the deceitful release and, at the same time, deny recovery to those who suffered only by their own lack of due diligence. In selecting the highest daily price the advantage works, to a greater degree, against TGS. But where, as here, the injury is suffered by an act making difficult the exact computation of damages, the wrongdoer is not heard to complain. For "it would be a perversion of fundamental principles of justice to deny all relief to the injured person, and thereby relieve the wrongdoer from making any amend for his acts." Story Parchment Co. v. Patterson Paper Co., 282 U.S. 555, 563 (1931).

In their cross-appeal, Reynolds and Mitchell also argue in favor of awarding attorneys' fees. We are cited to our decisions in Esplin v. Hirshi, 402 F.2d 94 (10th Cir. 1968), *cert. den'd* 394 U.S. 928 (1969), and Estate Counseling Service, Inc. v. Merrill Lynch, Pierce, Fenner and Smith, 303 F.2d 527 (10th Cir. 1962). It is contended that both decisions stand for the proposition that the policy in the federal courts is to award the costs of conducting the action

in securities cases. Although in both cases we allowed recovery of "other outlay legitimately attributable to the defendant's fraudulent conduct," it was not intended to include the costs of bringing the action. This is seen in the Estate Counseling Service case where a defrauded buyer brought the appeal but was not awarded attorney fees as "other outlay legitimately attributable to the defendant's fraudulent conduct." Attorneys' fees are denied.

The damages awarded to Reynolds amount to $12,687.50; Mitchell's damages are fixed at $7,600.00. The decisions by the trial court that both appellees are to receive interest computed at six per cent per annum from the time of sale until the date of the trial court's judgment, and that when recovery is gained from TGS, appellees' claims against Fogarty will be deemed paid, satisfied and discharged, are not disturbed.

Fogarty asserts on his own behalf that the trial court lacked personal jurisdiction over him. Section 27 of the Securities Exchange Act of 1934, 15 U.S.C. §78aa, provides that "[t]he district courts of the United States * * * shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce liability or duty created by this chapter or the rules and regulations thereunder. * * *" The remainder of that statute provides for service of process, allows for review of judgments and decrees, and designates proper venue. The latter provision relates back to the jurisdictional portion, and allows such actions to be brought in any district where the defendant is found or is an inhabitant or transacts business.

The brunt of Fogarty's allegations is directed at venue —not jurisdiction. His main claim is that he has never been an inhabitant of Utah, was not found in Utah, and transacts no business in that state. That was the identical issue posed to this court in Texas Gulf Sulphur Company v. Ritter, 371 F.2d 145, 148-49 (10th Cir. 1967), wherein

we said: "venue as to both defendants will lie in the Utah District if any of the acts or transactions complained of took place in that district." The acts and transactions complained of which have now been proved were "publication of news releases and acts incident to the sale of the stock referred to herein * * * the release of a false and fraudulent press release, upon which he [Reynold] relied after reading the same in the Wall Street Journal in Salt Lake City, which newspaper had been transmitted to him through the United States mails. In addition the plaintiff contends this press release came to Salt Lake City on the Dow-Jones broad tape." Thus the issue has been decided against Fogarty and is not now open to relitigation.

The only issue left to be decided is raised individually by Reynolds and concerns whether Rule 23 F.R.Civ. P., 28 U.S.C., should be applied to afford relief to all persons who sold TGS stock between April 12 and April 16, 1964. A number of independent inquiries are included in this argument, e.g., may an appellate court correct a class ruling after a decision on the merits; and may parallel class actions be conducted in two jurisdictions? But ignoring all collateral issues, as cross-appellant has invited us to do, the only issue is whether the trial court properly exercised its discretionary powers.

Rule 23(a) recites four prerequisites to a class action. Assuming, arguendo, that the elements of (a) have been met, it appears that the trial court was convinced that a class action in Utah would not conform to (b)(3) of Rule 23. That subsection requires, inter alia, that the class action be "superior to other available methods for the fair and efficient adjudication of the controversy." The Rule outlines four nonexhaustive matters which are to be considered in deciding the superiority of a class action: "(A) the interest of members of the class in individually controlling the prosecution or defense of separate actions;

(B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; and (D) the difficulties likely to be encountered in the management of a class action." In an opinion reported at 309 F.Supp. 566 (D.Utah 1970), the trial court denied the motion for a class action, basing the decision on Rule 23 (b) (3)(B), (C) and (D).

The trial judge recited that as of October 22, 1969, ninety-four actions had been brought against TGS and individual defendants; that in March, 1969, two actions in the Southern District of New York had been allowed to proceed as class actions; that pursuant to that ruling, tedious and time consuming discovery had taken place; and that if the various private suits were concentrated for trial in a single district, it should be in the Southern District of New York. In summary, he stated: "The litigation in New York is far advanced, far and away the bulk of the cases are there, and the information necessarily to be obtained from the brokerage offices is more readily and more conveniently available in New York City." Reynolds v. Texas Gulf Sulphur Company, 309 F.Supp. at 570. Our conclusion is that the trial court has wisely exercised its discretion.

In No. 280-70, the judgment is affirmed in all respects except as to the untimely sale of the 20 shares and as to the issue of damages. In No. 282-70, the judgment is affirmed in all respects except as to the issue of damages. Accordingly, No. 280-70 is remanded with directions to enter judgment for Mitchell for $7,600.00; and No. 282-70 is remanded with directions to enter judgment for Reynolds for $12,687.50. In No. 284-70, the judgment is reversed and the case is remanded with directions to enter judgment in favor of Texas Gulf Sulphur Company, et al. The cross-appeals in Nos. 281-70, 283-70 and 285-70, are denied.

Appendix A

Judgment of the United States Court of Appeals for the Tenth Circuit

MARCH TERM—APRIL 26, 1971

Before Honorable David T. Lewis, Chief Judge, and Honorable Delmas C. Hill and Honorable Robert H. McWilliams, Circuit Judges.

[SAME TITLE]

These consolidated cases came on to be heard on the record on appeal from the United States District Court for the District of Utah, and were argued by counsel. On consideration whereof, it is ordered as follows:

In case No. 280-70, the judgment of said district court is affirmed in all respects except as to the untimely sale of the 20 shares and as to the issue of damages.

In Case No. 282-70, the judgment of the said district court is affirmed in all respects except as to the issue of damages.

Accordingly, in case No. 280-70 the cause is remanded with directions to enter judgment for Mitchell for $7,600.00; and in Case No. 282-70, the cause is remanded with directions to enter judgment for Reynolds for $12,687.50.

In Case No. 284-70, the judgment of said district court is reversed and the case is remanded with directions to enter judgment in favor of Texas Gulf Sulphur Company, et al.

The cross-appeals in Nos. 281-70, 283-70 and 285-70, are denied.

/s/ HOWARD K. PHILLIPS

HOWARD K. PHILLIPS, Clerk.

Appendix A

Order of the United States Court of Appeals for the Tenth Circuit on Petition for Rehearing

JULY TERM—SEPTEMBER 10, 1971

Before Honorable David T. Lewis, Chief Judge, and Honorable Delmas C. Hill and Honorable Robert H. McWilliams, Circuit Judges.

Nos. 281-70 and 283-70

GEORGE GORDON REYNOLDS and WALTER A. MITCHELL,
Cross-Appellants,

v.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Cross-Appellees.

Cross-Appellant, Reynolds, has filed a Petition for Rehearing urging two points, neither of which goes to the merits of the case. First, he asks us to assess as costs in the case certain fees paid by him to expert witnesses. As a general rule, such fees in excess of the statutory allowance for fees, mileage and subsistence, are not taxable as costs. In some cases, courts, in the exercise of their general equitable powers, have permitted such allowances in cases involving exceptional circumstances, and in those cases the orders of allowance were made prior to time the witnesses testified. 6 Moore's F.P. 1367. In this case, the trial judge declined after trial to make such an allowance.

We are unable to conclude that the trial judge abused his equitable discretion in denying the allowance and affirm the trial judge in this respect.

By the second point, the petition asks us to supplement our opinion to expressly state that our denial of a class action for Reynolds does not preclude the possibility of other persons in the alleged class from bringing actions in any court having jurisdiction, either in their own behalf or under Rule 23. We see no necessity for such a supplement to our opinion and decline the request.

Accordingly, the petition for rehearing is denied.

Appendix B

Statutes and Rule Involved

Securities Exchange Act of 1934, Section 10(b), 48 Stat. 891, 15 U.S.C. §78j: "Regulation of the Use of Manipulative and Deceptive Devices":

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

"(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

Securities Exchange Act of 1934, Section 27, 48 Stat. 902, 15 U.S.C. §78aa: "Jurisdiction of Offenses and Suits":

"Sec. 27. The district courts of the United States, the District Court of the United States for the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this title or rules and regulations

thereunder, or to enjoin any violation of such title or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code as amended (U.S.C. title 28, secs. 225 and 347). No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts."

Rule 10b-5, 17 C.F.R. 240.10b-5: "Employment of Manipulative and Deceptive Devices":

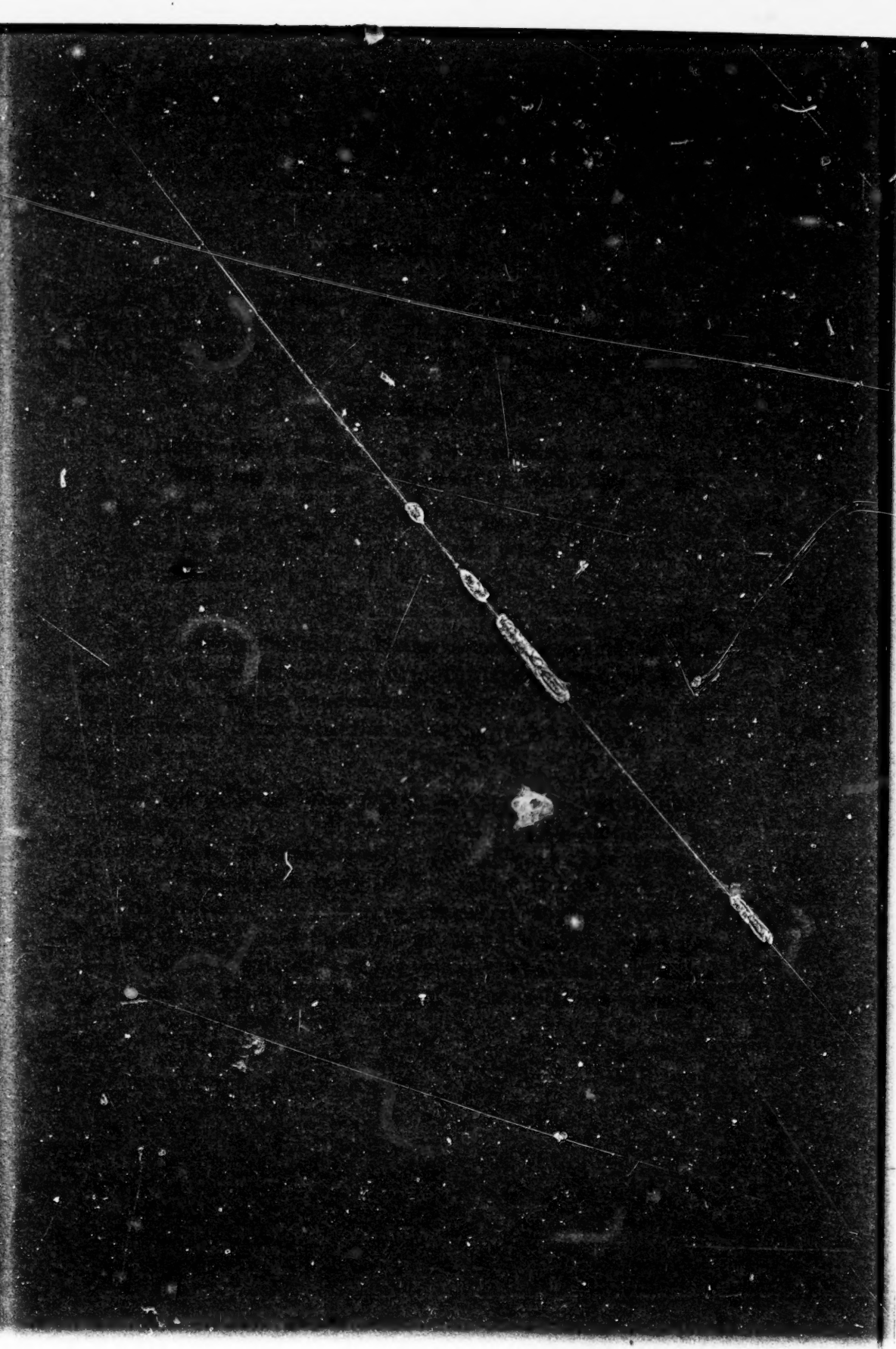
"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

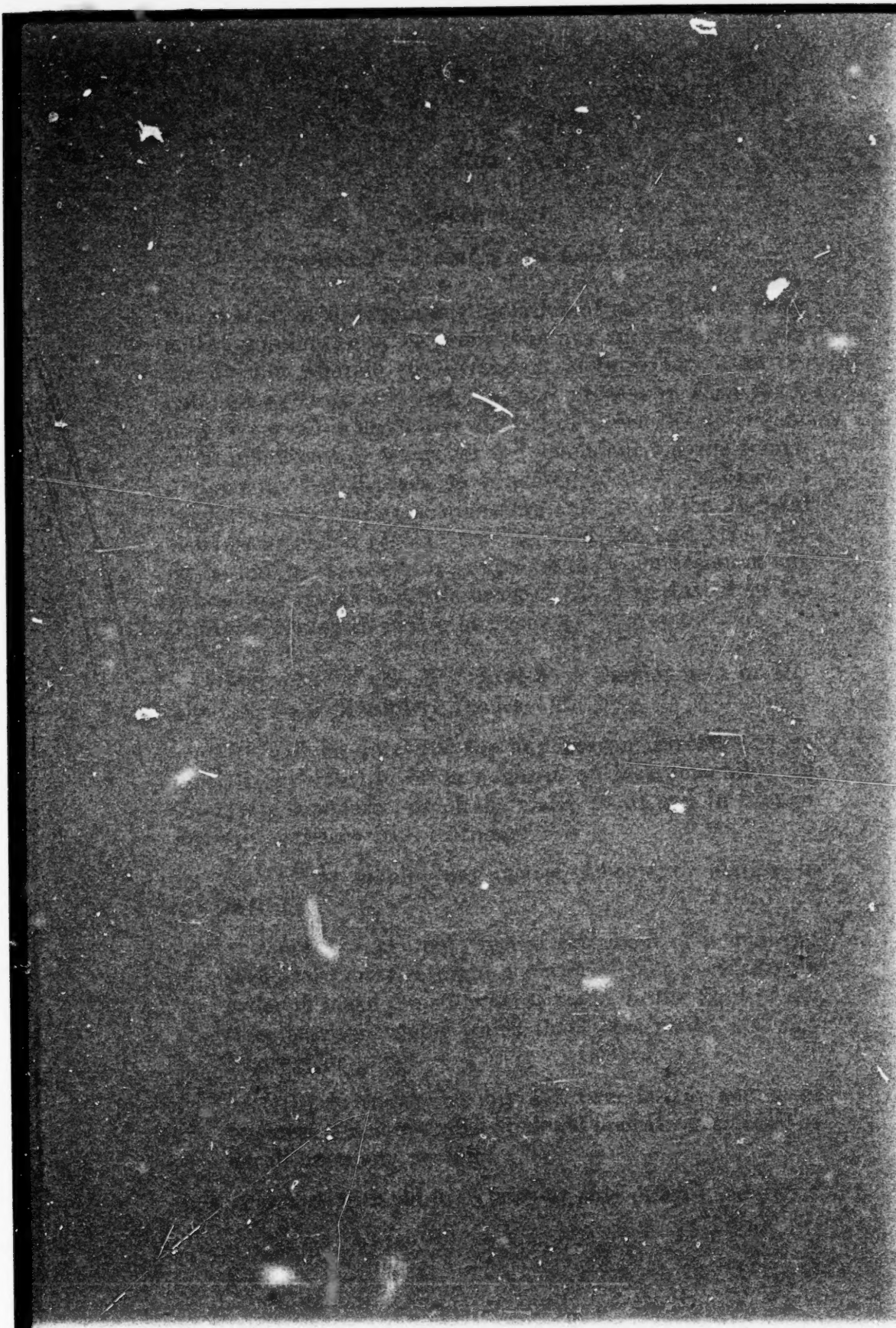
"(1) to employ any device, scheme, or artifice to defraud,

"(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

"(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security."





Appendix C

For the convenience of the Court, Item 8A(b), Schedule I to Form 1A relating to Regulation A offerings under the Securities Act of 1933 is set forth in this appendix.

Schedule I

Information Required to Be Included in the Offering Circular Required by Rule 256

The offering circular required by Rule 256 or statement required by Rule 257 shall be dated and shall contain the following information:

* * *

8A. *Mining business.* If the issuer is engaged or proposes to engage in mining or exploratory mining operations, briefly describe the business or proposed business of the issuer in accordance with the following instructions:

* * *

(b) Identify the principal metallic or other constituents of the deposits to be explored or developed and describe the characteristics of such deposits. No claim shall be made as to the existence of a body of ore unless it has been sufficiently tested to be properly classified as "proven" or "probable" ore, as defined below. If the work done has not established the existence of proven or probable ore, a statement shall be made that no body of commercial ore is known to exist on the property.

* * *

SUPREME COURT, U. S.

Supreme Court, U.S.
FILED
OCT 26 1971
E. ROBERT SEAVER, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-421

TEXAS GULF SULPHUR CO., ET. AL.,
Petitioners,

—v.—

WALTER A. MITCHELL, ET. AL.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-421

TEXAS GULF SULPHUR CO., ET. AL.,

Petitioners,

—v.—

WALTER A. MITCHELL, ET. AL.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR RESPONDENTS IN OPPOSITION

Respondents Walter A. Mitchell and George Gordon Reynolds submit their brief in opposition to the Petition for a Writ of Certiorari.

OPINIONS BELOW

The opinion of the United States District Court for the District of Utah is reported at 309 F. Supp. 548 and set forth

at page 1a of the Appendix to the Petition. The opinion of the Court of Appeals is not yet reported but is reproduced at page 40a of the Appendix to the Petition.

JURISDICTION

The judgment of the Court of Appeals was entered on April 26, 1971. A timely petition for rehearing was denied on September 10, 1971. The Petition for Certiorari was filed on September 23, 1971. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

QUESTIONS PRESENTED

1. Whether, in a cause of action based upon the federal securities laws, the Courts may judically add elements to the cause of action other than those specified by Congress and the Securities and Exchange Commission.

2. Whether the release of a false statement in financial news services is a sufficient use of facilities of interstate commerce, for the purpose of jurisdiction.

3. Whether the federal district court may properly fashion a rule of damages suitable to fraud in connection with the sale of securities in a rising market.

STATUTE AND RULE INVOLVED

The pertinent provisions of the Securities Exchange Act of 1934 (Exchange Act), and Rule 10b-5 adopted thereunder (17 C.F.R. 240.10b-5) (Rule 10b-5) are as follows:

15 U.S.C. §78j:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of

interstate commerce or of the mails, or of any facility of any national securities exchange—

• • •

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. §78aa:

The district courts of the United States, the district court of the United States for the Disrict of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this title or rules and regulations thereunder, or to enjoin any violation of such title or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found . . . .

Rule 10b-5:

It shall be unlawful for any person, directly or indirectly, by use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumsances under which they were made, not misleading or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

STATEMENT

On April 12, 1964 petitioners Texas Gulf Sulphur Company (TGS) and Charles F. Fogarty issued a statement to the news media discounting rumors concerning its mineral explorations near Timmins, Ontario, Canada which had reportedly leaked out because of large purchases of TGS stock by corporate insiders (deceptive release). Four days later, on April 16, 1964, TGS confirmed the discovery of a mine at Timmins which has since proven to be one of the most spectacular mining discoveries in history (corrective release). All of the essential information contained in the April 16 release was based upon exploration which had been completed prior to April 12, 1964, and a materially significant portion of which had been available to TGS since November of 1963.

Respondents were shareholders in TGS on April 12, 1964 who sold their stock on the morning of April 16, before the corrective release was communicated to them or was reasonably available to members of the investing public. They claimed that the April 12 release, in light of the disclosures contained in the corrective release, was materially false and misleading and that the deceptive release caused them to sell their stock.

The trial judge entered judgment for the plaintiffs and held that because of the peculiar facts of a fraudulently induced sale of stock in a rapidly rising market, damages should be

calculated according to the difference between the price at which the plaintiffs sold and the average market price of TGS shares during 20 trading days following the sale, reasoning that the impact of the disclosure of the corrective release was felt by the market during that period of time. The Court of Appeals affirmed, but modified the damage award by requiring that damages be calculated according to the market high during the 20 succeeding trading days rather than the average during those trading days. The Court of Appeals reasoned that calculating damages according to the market high was desirable in the interest of providing maximum deterrence to securities fraud.

Petitioners incorrectly state that Respondents "sales had taken place *after* dissemination of the second press release" (emphasis by Petitioners). The key word here is "dissemination," and on uncontroverted evidence both the trial judge and the Court of Appeals concluded that the second press release had not been "disseminated" in the sense that it was not reasonably available to Respondents or to members of the investing public. Indeed, as to the sale of Respondent Reynolds, he instructed his broker to sell prior to the time when the corrective release had even been delivered to the news media. Respondents seek to make capital of the time lag between when the sell order was delivered and when trades were technically negotiated on the stock exchange, located thousands of miles away, at a time subsequent to the precise moment when the corrective release went out on the Dow Jones wire service.

ARGUMENT

The decision of the Court of Appeals, other than with respect to the question of class action treatment,* is correct. No

---

* Respondents intend to separately petition this Court for review of the Court of Appeals treatment of the class action, within the time per-

conflict is presented, and the decision presents no important questions which merit review by this Court.

A. Review by this Court of the question of the nature, scope and extent of liability under section 10(b) of the Exchange Act (15 U.S.C. §78j) and Rule 10b-5 would be superflous. These very questions are presented in *Manhattan Casualty Co. v. Bankers Life and Casualty Co.*, Docket No. 70-60 (October Term, 1971) and *Affiliated Ute Citizens v. United States*, Docket No. 70-78 (October Term, 1971), both of which are now submitted on the merits and awaiting decision. Any guidance to the lower federal courts which is considered either appropriate or necessary on the questions of the proper connection between an allegedly fraudulent act and a securities transaction, or the propriety of "privity, short statutes of limitation, *scienter*, causation and undertakings for costs" (Pet. 18) will undoubtedly be supplied in either or both of said matters presently awaiting decision. Furthermore, Petitioners unabashed proposal that this Court should import restrictive provisions of other securities laws into Rule 10b-5 (Pet. 18-20) would emasculate the intent of Congress, for these other securities laws contain substantially different terminology. Thus, section 17(a) of the Securities Act of 1933 (15 U.S.C. §77q (a)) requires that the wrongful practices be "in the offer or sale" of securities, while section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. §78j) employs the much looser linkage "in connection with the purchase or sale of any security." The requirement of "reliance" was written into section 11(a) of the Securities Act (15 U.S.C. §77k(a)), and section 18 of the Exchange Act (15 U.S.C. §78r) includes a requirement of *both* reliance and scienter. *Neither* requirement was incorp-

---

mitted by law. The class action is thought to be a matter of national importance, in that the 1966 amendments to Rule 23 have never been construed by this Court and present important questions of judicial efficiency.

orated in section 10(b), and to say that either requirement should be added by judicial construction, in the face of Congress' calculated use of these terms in other contexts in the same legislation, would be improper.

B. The question of jurisdiction over Petitioner Fogarty under provisions of Section 27 of the Exchange Act (15 U.S.C. §78aa) was decided correctly, and in accord with a large body of precedent under the Exchange Act. See 3 Loss, SECURITIES REGULATION 1523 (2d Ed. 1961):

> ". . . the mailed matter need not even be addressed to a victim; the misstatements may be made orally and the mails used by the defendants merely in communicating among themselves. Similarly, it suffices if the mails (or, under the SEC provisions, interstate facilities) are used only in making or postponing an appointment with the victim, or making an offer, or acknowledging receipt of an order, or confirming a transaction, or having a broker sell the securities fraudulently obtained.
>
> "Moreover, the use of the mails by the particular defendant may be indirect. Since the mail fraud statute covers anybody who 'knowingly causes [any matter or thing] to be delivered by mail' and all the SEC fraud provisions contain the phrase 'directly or indirectly,' it suffices to show that the defendant caused another person to use the mails or might reasonably have foreseen that their use would occur." (citations omitted)

Accord, Ellis v. Carter, 291 F. 2d 270 (9th Cir. 1961); *Matheson v. Armbrust,* 284 F. 2d 670 (9th Cir. 1960) *cert. denied* 365 U.S. 870 (1961); *Hooper v. Mountain States Securities Corp.,* 282 F. 2d 195, 204-05 (5th Cir. 1960) *cert. denied* 365 U.S. 814 (1961); *Fratt v. Robinson,* 203 F. 2d 627 (9th Cir. 1953).

C. The measure of damages adopted by the Court of Appeals is a reasonable one, and presents no question of na-

tional importance which should be reviewed by this Court. The statement of Petitioners that Respondents, who purchased their stock many years before at prices substantially lower than prevailed in April, 1964, "did not lose money" (Pet. 26) simply ignores the obvious. Moreover, this question is also awaiting decision in *Affiliated Ute Citizens v. United States*, Docket No. 70-78 (October Term, 1971). We subscribe to the SEC's statement of the proper measure of damages at page 58 of its *amicus curiae* brief in the *Affiliated Utes* case:

> "The measure of damages should always be at least equal to the plaintiff's loss – that is, the difference between the price he received and the price he would have received had there been no fraudulent conduct (usually the fair market price). A measure of damages based upon the profits, if any, realized by the defendant is appropriate . . . if that amount is greater than the plaintiff's actual loss, the theory in such case being that the shares are held in constructive trust for the plaintiff and that the defendant should not be enriched by his wrongdoing. *Janigan v. Taylor*, 344 F. 2d 781 (C.A. 1), certiorari denied, 382 U.S. 879."

This Court has taught that "where legal rights have been invaded, and a federal statute provides for a general right to sue for such invasion, federal courts may use any available remedy to make good the wrong done." *J. I. Case Co. v. Borak*, 377 U.S. 426 (1964). Consistent with that admonition, the Court of Appeals fashioned a damage measure suitable to the peculiar problems of a fraudulently induced sale of stock in a rapidly rising market. No conflict with established damage law is presented. *Compare, Galigher v. Jones*, 129 U.S. 193, 201 (1889).

D. The Court of Appeal's application of the state statute of limitations governing fraud actions, rather than the shorter statute of limitations contained in the state blue sky law, is

consistent with the weight of authority. *E.g. Charney v. Thomas*, 372 F. 2d 97, 99-100 (6th Cir. 1967):

> "Because of the remedial nature of the Blue Sky Law, it should be taken to provide an added cause of action for the defrauded plaintiff, rather than the only one.
>
> • • •
>
> "While several courts have considered the question of a limitation period for federal securities fraud actions under section 10(b), none has applied the provisions of the local Blue Sky Law in this regard."

Vanderboom v. Sexton, 422 F. 2d 1233 (8th Cir.) *cert. denied* 400 U.S. 852 (1970) relied upon by Petitioners (Pet. 27) stands alone as an anomaly in the law. Against the weight of cases in accord with the Court of Appeals herein, it does not present a conflict meriting the attention of this Court.

CONCLUSION

For the foregoing reasons, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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IN THE

Supreme Court of the United States

October Term, 1971

Docket No. 71-421

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

WALTER A. MITCHELL,
Respondent.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

GEORGE GORDON REYNOLDS,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

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IN THE

Supreme Court of the United States

October Term, 1971

Docket No. 71-421

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

WALTER A. MITCHELL,
Respondent.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

against

GEORGE GORDON REYNOLDS,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITIONERS' REPLY BRIEF

Opinion Below

The decision below has now been officially reported at 446 F. 2d 80.

Introductory Statement

There appear to be discrepancies in the facts cited to this Court by petitioners and those contained in the Brief for Respondents in Opposition (hereafter "Res. Br.").

These discrepancies relate to the nature of Texas Gulf's press releases of April 12 and April 16, 1964 and the timing of respondents' sales of stock in relation to the second release. These apparent discrepancies are easily resolved by reference to stipulated or otherwise undisputed facts contained in the record below.

Respondents assert that "all the essential information" contained in Texas Gulf's press release of April 16, 1964 "was based upon exploration which had been completed prior to April 12, 1964", and that "a materially significant portion * * * had been available to TGS since November of 1963" (Res. Br., p. 4). The November information referred to was a single 1¼" drill core 655 feet in length, a description of which comprised part of the April 16 release (4a, 42a).

Facts stipulated by the parties show that the April 12 release, which contained no details of drilling results, was prepared at a time when the draftsmen of the release had available reports on 2,804 feet of drilling; when the April 16 release was prepared, reports on 5,257 feet of drilling were available. The dispute between the parties does not relate to what information was available, but rather what the law required Texas Gulf to say in light of that information when it commented on the rumors which were then circulating, and whether respondents have a claim for damages based on what was said.

Another discrepancy would appear to surround the timing of respondents' sales with respect to the availability of information contained in the April 16 release. It is un-

controverted that at approximately 8:00 A.M.* on April 16, 1964, that release was issued to the news media. It was stipulated that at 8:29 A.M. the brokerage firm used by Reynolds in Utah received a teletype reporting Texas Gulf's announcement of a major discovery. It was stipulated that a Dow-Jones news wire appeared on the broad tape in all brokerage houses in the country by 8:55 A.M., announcing a major discovery of 25,000,000 tons of ore, and that a supplement to that report had been received by 9:02 A.M.

Mr. Reynolds testified that at 8:45 A.M. or 9:00 A.M. on April 16 his broker called and advised him of a rumor that Texas Gulf had made a big strike. The brokerage house record revealed that Mr. Reynolds' order to sell was placed in Salt Lake City at 9:10 A.M. When the first order could not be consummated, Reynolds and his broker spoke again, and a second order was placed at 9:23 A.M., and the transaction closed at 9:31 A.M.

It was stipulated that Mitchell's first order was placed at 12:40 P.M., some three and one-half hours after his Los Angeles brokers received and posted the Dow-Jones announcement of Texas Gulf's discovery. His order to sell was placed several points above the then market, and could not be consummated until the following day when his specified price was first reached upon the stock exchange auction market.

There may be a dispute as to whether these respondents actually knew about the April 16 release when they sold. But stipulated facts fix the availability of that information to both of them well before either sale order was placed,

* All times referred to are Mountain Standard Time.

and the petitioners' contentions do not in any degree turn upon any "time lag between when the sale order was delivered and when trades were technically negotiated," as respondents suggest (Res. Br., p. 5). See Petition, pp. 23-24.

Discussion in Reply

A.

Respondents state that the petition presents no important questions which merit review by this Court. Their position is premised upon the proposition that the questions here raised will be decided by this Court in its consideration of *Manhattan Casualty Co.* v. *Bankers Life & Casualty Co.*, Docket No. 70-60 (Oct. Term, 1971) and *Affiliated Ute Citizens* v. *United States,* Docket No. 70-78 (Oct. Term, 1971).* This is simply not the case. While both of those appeals present significant questions with respect to the interpretation and application of Rule 10b-5, neither presents the wide range of issues nor has the far-reaching significance and consequences of this case and the companion case of *SEC* v. *Texas Gulf* (Docket Nos. 327, 328, 346, 347).**

Both *Manhattan Casualty* and *Affiliated Ute Citizens* involved schemes to defraud, schemes designed to benefit the defendants at the expense of the particular plaintiffs. The instant case involves the issue of liability of a cor-

* The Circuit Court decisions in these cases are reported at 430 F.2d 355 (2d Cir. 1970) and 431 F.2d 1349 (10th Cir. 1970).

** We urge that this Court consider this petition in conjunction with the petitions in the *SEC* action. Both cases involve the same factual setting, and several of the legal principles first announced in the *SEC* case were applied by the Tenth Circuit below within a different legal context. The Solicitor General's Brief in *SEC* v. *Texas Gulf* is scheduled to be filed by November 8, 1971.

poration and its officers to potentially thousands of persons with whom they had no business dealings, and from whom they took no property and acquired no benefit. The present case does not arise from a scheme to defraud anyone, but rather from an attempt with laudable motives to warn the public of extravagant rumors.

The present case and the *Manhattan Casualty* and *Affiliated Ute Citizens* cases do involve the same administratively promulgated regulation, and some of the same clauses of that regulation, particularly the requirement that the fraud be "in connection with the purchase or sale of any security." But there the similarity ends. *Manhattan Casualty* presents the questions of whether a person must be a purchaser or seller of securities to maintain a private action under Section 10(b) and Rule 10b-5, and whether the "in connection with" requirement is satisfied when the scheme is to loot the assets of the corporation and the proceeds of a sale of securities are diverted, where neither the purchaser nor the seller was deceived in the securities transaction. The question under Rule 10b-5 (as distinct from questions under the Indian statute) presented in *Affiliated Ute Citizens* v. *United States* involves the liability of persons aiding or abetting persons benefiting in a fraudulent securities transaction, although not themselves purchasing. Neither case presents the broad and important questions of *scienter,* reliance, causation, damages and statute of limitations here present, nor the broad and basic policy issues involved in the publication of information of interest to business, stockholders and the public at large by a company which is not dealing in or attempting to influence the price of securities. It would be in the public interest for the Court to address itself at this time not only

to the important questions presented in the *Manhattan Casualty* and *Affiliated Ute Citizens* cases, but also to the far broader questions presented in this case and in *SEC* v. *Texas Gulf*.

Respondents further contend that the thrust of this petition for certiorari is to suggest that this Court should import restrictive provisions of other securities laws into Rule 10b-5, and that to do so "would emasculate the intent of Congress." While Congress expressly provided private rights of action under the statutes referred to by respondents (Res. Br., p. 6), a private right of action under Section 10(b) and Rule 10b-5 was not so provided, and that right of action has been judicially created by the lower federal courts. The elements which must be proved in establishing a private right of action not created by Congress is the issue before this Court.

The statute and rule as drafted are predicated upon "manipulative and deceptive devices" and "fraud and deceit." Rather than suggesting the addition of restrictions from other sections of the securities laws, petitioners' position is that the statutory and regulatory language should be given its clear meaning, and that in order to recover damages under Rule 10b-5, a plaintiff should be required to prove intentional or knowledgeable wrongdoing in connection with a securities transaction, and that some of the elements of an action for fraud or deceit are present; that is, there was at least a false representation of a material fact made with intent to deceive, upon which plaintiff reasonably relied and was caused damage thereby. These elements are incorporated into the securities law provisions to which petitioners referred, evidencing the intent of Congress that liability would not be unlimited. Dispensing with

these basic elements as respondents suggest would effectively negate Congressional intent expressed in the carefully drawn legislation.

B.

The precedents cited by respondents to support jurisdiction over Dr. Fogarty in the District of Utah (Res. Br., p. 7) do not reach the question here presented. Each of those cases involved deliberate use by the defendant of facilities within the forum state in the course of a securities transaction. Dr. Fogarty engaged in no such purposeful activity within Utah as the Constitution requires.

C.

Respondents also argue that the question of the measure of damages should not be reviewed by this Court, that it is not a question of national importance. Yet it can affect the financial viability of corporations in every state in this nation.

With the burgeoning increase of Rule 10b-5 suits and class actions,* the question of damages to be awarded is of importance to the management of every publicly-held corporation which may conceivably be called upon to issue a press release on a matter of importance to shareholders or to the public, and to other corporations, accountants, and

* Indeed, this Court has been advised not only that respondents will separately petition this Court for review of the treatment of this case as a class action (Res. Br., pp. 5-6, n.), but also of the pendency of another class action involving Texas Gulf's press release. The Tenth Circuit noted that if its damage measure were adopted, liability could amount to millions of dollars (66a-67a n.). Just the differential between the damage measures applied below by the District Court and the Court of Appeals can in a class action mount into the millions, and it alone presents to this Court a question requiring review.

businessmen, etc., caught up in the myriad of charges brought under Rule 10b-5. This question is of equal importance to investors everywhere who could find themselves paying monumental judgments through their ownership of stock in a defendant corporation. The investments of one group of shareholders, who retained their stock in the company, are depleted by payments to identically situated shareholders who sold, even though the corporation or its shareholders did not receive and did not intend any benefit from the corporate action.

The authorities cited by respondents on the damage issues are not in point. This is neither a case of conversion (*Galigher* v. *Jones,* 129 U.S. 193 (1889)), nor a case where defendants reaped profits which should in justice be returned to plaintiff (*Janigan* v. *Taylor,* 344 F.2d 781 (1st Cir.), *cert. denied,* 382 U.S. 879 (1965)). Texas Gulf did not profit from the issuance of the April 12 release; and respondents received for their stock the prevailing market price reflecting the judgment of the investing public following issuance of Texas Gulf's April 16, 1964 release. Respondents received for their stock higher prices than obtained prior to the issuance of the press release of which they complain. The Securities Exchange Act provides only for the recovery of "actual damages" (15 U.S.C. §78bb (a)); here respondents suffered none.

D.

In *Charney* v. *Thomas,* 372 F.2d 97 (6th Cir. 1967) (Res. Br., p. 9), the Sixth Circuit Court of Appeals observed that "in some cases the local Blue Sky Law might be the more appropriate point of reference", but that in that

case Michigan law contained "no provision similar to section 10(b) of the federal law." *Id.* at 100. Thus the court applied Michigan's fraud statute of limitations. But Utah's Blue Sky provisions contain language almost identical to Rule 10b-5, and if the elements of fraud are to be dropped from Rule 10b-5 actions, fraud statutes of limitations have no applicability. The conflict of the decision below with *Vanderboom* v. *Sexton,* 422 F.2d 1233 (8th Cir.), *cert. denied,* 400 U.S. 852 (1970), also warrants review.

Conclusion

It is respectfully requested that this petition for a writ of certiorari be considered in conjunction with the companion petitions in *SEC* v. *Texas Gulf Sulphur* (Docket Nos. 327, 328, 346, 347), and that all such petitions be granted for the reasons set forth therein.

Respectfully submitted,

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November 3, 1971

IN THE

Supreme Court of the United States

October Term, 1971

No. ~~421~~ 71-421

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

v.

WALTER A. MITCHELL,
Respondent.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

v.

GEORGE GORDON REYNOLDS,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITION FOR REHEARING

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IN THE

Supreme Court of the United States

October Term, 1971

No. 421

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

v.

WALTER A. MITCHELL,
Respondent.

TEXAS GULF SULPHUR COMPANY and CHARLES F. FOGARTY,
Petitioners,

v.

GEORGE GORDON REYNOLDS,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITION FOR REHEARING

Petitioners respectfully move this Court for an order (1) vacating its denial of their petition for certiorari, entered on December 20, 1971, and (2) granting the petition. In support of this motion, petitioners state the following:

I

This petition may be considered by the full Court of nine Justices.

The petition for certiorari was denied on December 20, 1971, with Justices Stewart and Blackmun dissenting. At the same time, petitions were also denied in *SEC* v. *Texas Gulf,* Docket Nos. 327, 328, 346 and 347. Petitions for rehearing are also being filed in those cases. Since that time, two new Justices have become members of this Court.*

There is pending before this Court a petition by George Gordon Reynolds and Walter A. Mitchell arising from this same case. (Docket No. 693) That petition will be considered by the full Court, and we respectfully submit that the instant petition and the underlying petition for certiorari should be considered by the full Court at the same time.

There can be no question of the importance of the questions presented in this case and in the *SEC* case and of their significance for the future administration of the securities laws.

It is respectfully urged that the entire Court consider the issues presented by the petition for certiorari. The issues are of first impression and of great public importance. In addition, we submit the following additional reason for review.

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* While Rule 58(1) of this Court provides that a petition for rehearing of judgments or decisions other than those denying or granting certiorari "will not be granted, except at the instance of a justice who concurred in the judgment or decision and with the concurrence of a majority of the Court," no such restriction appears in subdivision (2) relating to petitions for rehearing of denial of certiorari. Similarly, the practice for new Justices not to participate in the consideration of a petition for rehearing after a decision on the merits would not seem to apply to the consideration of a petition for rehearing of denial of certiorari. *Cf.* STERN & GRESSMAN, SUPREME COURT PRACTICE §§15.6 and 15.7 (4th ed. 1969).

II

The commencement of a new class action and the settlement of other private litigation arising out of the facts of this case forcefully demonstrate the importance of review by this Court of the rules governing disclosure under the securities laws.

Since the date of the denial of the petition for certiorari, two significant intervening events have occurred to which petitioners would like to draw the attention of this Court:

1. On December 30, 1971, there was filed in the Southern District of New York an Agreement of Compromise and Settlement which proposed a settlement of the bulk of the Texas Gulf private litigation pending in that court and in the New York state court.*

2. On January 11, 1972, an action entitled *Fox* v. *Texas Gulf Sulphur Company* (Civil No. C-1872) was filed in the District of Utah, with respondents' attorney appearing as attorneys for plaintiff there. This is an alleged class action brought by a person who claims to have sold 40 shares of Texas Gulf stock in reliance upon the April 12 press release, but after the second (April 16) press release announcing a major ore discovery had appeared on the Dow-Jones broad tape and had been received in every brokerage office in the country. Plaintiff seeks recovery of at least $10,000,000 for himself and for members of the alleged class, which is defined to include: (1) all sellers on April 16 after 10:55 A.M., when the Dow-Jones broad tape carried

* This proposed settlement is referred to in the Reply Brief (p. 4) filed by the petitioners in *Reynolds and Mitchell* v. *Texas Gulf Sulphur*, Docket No. 693, which is to be considered by the entire Court.

the second Texas Gulf press release, and (2) all sellers on April 17, 1964, or "until such later time as public investors in such stock had a reasonable opportunity to acquaint themselves with and act upon the information contained in the April 16, 1964 press release of TGS."

These two events in juxtaposition demonstrate the hazard to which the management and shareholders of a publicly held company may be subject for an innocent act under the rules of law announced by the courts below. The operative terms of the proposed settlement call for the payment in escrow of $2.7 million by Texas Gulf. Of this amount, $2.2 million is allocated for payment of the claims asserted in a class action on behalf of those who claim to have sold Texas Gulf stock in reliance upon the April 12 press release prior to the time that the second release announced the Timmins discovery. A hearing is scheduled for March 9, 1972 to determine whether this settlement should be approved.

Despite this settlement (which does not encompass the present action or the *Fox* action) petitioners are still being subjected to huge claims of damages based on the April 12 release. There were approximately 325,000 shares of Texas Gulf stock sold on April 16 after 10:55 A.M., and approximately 500,000 shares sold on April 17. Recovery is sought in the new alleged class action on behalf of twice again as large a class as the actions just settled. As pointed out in the petition herein (pp. 23-26), the Tenth Circuit refused to limit liability emanating from the April 12 release to those who sold prior to the time (10:55 A.M. on April 16) that petitioners' second release became available in every brokerage house in the country. The filing of the alleged

class action at this time underlines the importance of review of both the measure of recovery and the period of damage exposure announced by the Tenth Circuit, as well as the new underlying theories of that decision.

The decisions below, upon which plaintiff Fox will undoubtedly rely, ordered Texas Gulf to pay damages on the basis of a record which contained not a shred of evidence of conscious wrongdoing by Texas Gulf.* Not only was Texas Gulf not benefited in any way by the release, but there was not even a theory advanced as to how the release could have been monetarily beneficial to Texas Gulf. Despite this, innocent shareholders who held or bought Texas Gulf shares were required to pay to selling stockholders additional "profits" those sellers might have made had they not sold their shares at the particular time.

The basic issue below was whether Texas Gulf had a legal duty to say more than it did when it issued a wait-and-see statement on April 12, 1964. This issue was resolved without the benefit of any statute or SEC regulation prescribing standards for voluntary public statements in response to false and exaggerated rumors. If every statement issued by a publicly-held company is to be subjected to *ex post facto* judicial scrutiny befitting a prospectus, and if liability for failure to pass this scrutiny extends to the world of buyers and sellers of such securities for an indefinite period of time, that is a matter of grave importance for the shareholders and management of such

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* It is noteworthy that respondents' answering brief did not question petitioners' statement that the record contains no evidence upon which a finding of intent to deceive could be based.

companies. Rather than countenance the establishment of new doctrine through the traumatic process of novel judicial interpretation of a statute enacted in 1934 and of long standing administrative regulations, this Court should urge those who seek to impose new duties on corporate management to utilize the procedures provided for rule making and legislation. See *Reliance Electric Company* v. *Emerson Electric Company,* 40 U.S.L.W. 4125 (U.S. Jan. 11, 1972).

Petitioners respectfully submit that the above described events give concrete support to the concerns previously voiced by petitioners. It should be for this Court to determine whether the Congressional purpose is furthered by decisions which, by imposing exacting *ex post facto* standards and extending damage exposure to thousands upon thousands of investors, discourage good faith disclosure and bring about "large judgments, payable in the last analysis by innocent investors, for the benefit of speculators and their lawyers * * *." *Securities and Exchange Commission* v. *Texas Gulf Sulphur Company,* 401 F.2d 833 at 867 (2d Cir. 1968) (Friendly, J. concurring).

Conclusion

For the reasons set forth above, as well as those contained in the petition for a writ of certiorari in this action and in the companion petitions in Nos. 327, 328, 346 and 347, petitioners pray that this Court grant rehearing of the

order of denial and grant review of the judgment and opinion below.

Dated: January 14, 1972

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Certificate of Counsel

As counsel for the petitioners, I hereby certify that the petition for rehearing is presented in good faith and not for delay, and as described above, is restricted to the grounds specified in Rule 58(2).

/s/ ORISON S. MARDEN

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